Los Angeles lawyers Edward Casey and Andrea Warren examine ballot initiatives affecting land use in Los Angeles.
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During World War II, the U.S. Office of War Information coined the phrase “loose lips sink ships” for propaganda posters reminding the public that careless conversation could provide useful information to enemy spies. Seventy-five years later, the phrase could be “loose e-mails sink campaigns.” Setting aside whether the Russians or WikiLeaks or both hacked Hillary Clinton’s State Department e-mails or those of her presidential campaign or the Democratic National Committee, an unequivocal question begs asking: Why send, much less write, messages containing insulting comments or disclosing key strategic decisions in the first place?

Some e-mails, Clinton told Jimmy Kimmel, were “so boring.” In one titled “Gefilte fish,” she asked, “Where are we on this?” In a second, she wanted to know the show times for “Parks and Recreation” and “The Good Wife.”

The same, however, hardly applies to those sent by campaign staff or supporters. John Podesta, Clinton’s campaign chairman, wrote a message describing Senator Bernie Sanders as a “doofus.” Neera Tanden, a Clinton supporter, said in a message titled “Hillary,” “Her instincts are suboptimal.”

Clinton and the Democrats are not alone in exercising questionable judgment. After Sony Pictures computers were hacked several years ago, messages from studio co-chair Amy Pascal were released disclosing her unflattering comments on, among others, former President Barack Obama, Aaron Sorkin, and Cameron Crowe.

Attorneys would be well advised to heed the following tips from the March 2015 issue of the New York Legal Ethics Reporter on best practices in using e-mails:

1. Never respond to any message without thinking of the consequences of that communication becoming public.
2. Remove excessive “strings” of messages . . . and include only what’s necessary.
3. Remove attachments unless necessary. Never send an email message without knowing exactly what’s on every page of an attachment. Consider stripping metadata . . . or sending a PDF or facsimile version of the document.
4. Rename messages when appropriate.
5. Turn off the “Suggest Names” option to avoid automatically filling in the wrong name. . . .
6. Consider drafting email messages without the “To,” “Cc,” and “Bcc” fields being completed until after your message is drafted, and you are sure it’s complete. This will avoid the transmission of messages to anyone unless you are absolutely sure that they are the intended recipients.
7. Hitting “Reply to All” is always a disfavored practice . . . .
8. If you are a recipient of a “Bcc” message, do not hit “Reply to All” . . . you may be disclosing something that the sender intended to keep confidential.
9. Clean out your Inbox by filing or printing relevant messages and deleting extraneous messages. . . .
10. Take a deep breath . . . [w]atch your language and grammar. Remember: Nothing is funny when it’s used as an exhibit in a lawsuit, or as an example of poor judgment or violation of policy. (Emphasis in original.)

When all else fails, consider the Yiddish word sechel (common sense) and remember that today any reasonable expectation of privacy no longer exists.
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Laura A. Wasser  Attorney

What is the perfect day? I go for a run, make breakfast for my kids, work with clients, and leave work in time to have dinner with my kids.

You are a family law lawyer. What is the most important part of that job? Problem solving in a way that fits legally and emotionally into the clients’ expectations.

How do you accomplish that? Having realistic expectations at the outset; if someone is very litigious, we will refer them to someone else. We are settlement-oriented.

What if the other side is not cooperative? That’s when I love going to court, because our family law judges are really smart and recognize a reasonable position.

You have been called the Disso Queen. Are you? I don’t know why I’m called the disso queen. I can’t seem to shake it.

Are prenuptial agreements the first stage of a celebrity marital cycle? A prenuptial makes sense for a high earner, especially if the earning continues as a result of what he or she did before marriage. They don’t want the State of California controlling what they do with their wealth.

Have you seen couples break up over the prenuptial agreements? Not often, but I’ve had some very uncomfortable and unpleasant negotiations. Once they are at the end of it, though, the relationships are healthier because they have a much better understanding of each other.

Many prenuptial agreements also contain a confidentiality agreement. How do you protect privacy? Put teeth in the contract—something like $100,000 for every breach.

What can be done to promote privacy? Change California law to make divorce filings private or anonymous. That’s how it is in New York. I am a big proponent of the First Amendment but I don’t understand how the benefit to the public outweighs the detriment to private individuals.

Paparazzi are all over celebrity divorces. Can you avoid them? People who are famous sign up for this, but they usually think of the red carpet. When you’re going into the courthouse for a custody hearing, it totally sucks. We try to do as much as we can out of the public forum.

TMZ splashes the news of a divorce filing within the hour. How? If you’re at the courthouse, you can immediately get a look at that file. If you grease the right person, you get the file sooner.

What motivated you to write your book, It Doesn’t Have to Be That Way? It’s a guide to making it nicer, particularly if you have kids. Divorce is unlike other litigation, because this person is someone you’re going to be dealing with for a very long time. He or she is your family member.

What are the qualities that are the same between most divorcing couples? They are sad, scared, and angry.

Are there differences within specific categories of celebrities? I notice that musicians are emotional, athletes like a game plan, and actors do well with a script.

What is the biggest difference between celebrity divorces and those of everyday folks? Someone telling you no.

What are the qualities that are the same between most divorcing couples? They are sad, scared, and angry.

Are there differences within specific categories of celebrities? I notice that musicians are emotional, athletes like a game plan, and actors do well with a script.

What motivated you to write your book, It Doesn’t Have to Be That Way? It’s a guide to making it nicer, particularly if you have kids. Divorce is unlike other litigation, because this person is someone you’re going to be dealing with for a very long time. He or she is your family member.

Are you writing a second book? No. I am launching an app in 2017, which will enable people to go online for help and live chat. The app is called itsovereasy.com. Right now, it’s a blog.

Your initials spell LAW. Coincidence? When my parents learned that my father passed the California bar, they celebrated by having sex. When they found out my mother was pregnant, they did the math and decided to name me Laura Allison Wasser.

Who do you turn to for advice? My parents.

Are they still married? No, but they had a good divorce.

What is the one characteristic you most admire in your mother? Her positivity.

You went to UC Berkeley for undergraduate school. What did you study? Rhetoric.

You graduated from Loyola Law School in 1994. Why did you want to become a lawyer? I am a problem solver who enjoys looking at two sides of a conflict to find a resolution.

Were you frightened when you first appeared in front of a judge? Of course.

You were a consultant on Liar, Liar, a
Movie starring Jim Carrey as an attorney who had to tell the truth. Is that hard for lawyers to do? I don’t think it is. All you have is your word.

You are currently unmarried. It is said you prefer to be unmarried. Has your work impacted your view of marriage? Probably.

Marriages rates have been declining for decades. Do you think marriage is on its way out? Certainly not in Los Angeles—we love a romance.

California is among nine other community property states. Do you think community property laws are fair? Fair is a very subjective term. I feel if both parties are aware of the law in the state where they reside and opt to enter into a marriage contract based on those laws, community property is fair. Obviously, in certain circumstances, a community property structure doesn’t seem to make sense. That’s where prenuptial agreements can be most helpful.

Equitable distribution states claim their system is fair. Do you agree? Equitable distribution states must rely on their judicial officers to apply the law fairly based on the circumstances involved.

Studies say 30 to 60 percent of spouses cheat. How often is it a factor in divorce? It can be a factor but not the determinate cause.

Are you involved in a charitable organization? The Harriet Buhai Center for Family Law and A Place Called Home. I am raising two Los Angelenos in an environment in which they can learn and thrive. I find it totally unacceptable that there are children in our city who have so much less.

What is your hidden talent? How hidden does it have to be?

What was your last vacation? I took the kids to Italy for three weeks.

What is your greatest vanity? High heels.

What are three deplorable world conditions? The water situation, the judgmental nature of people, and the bipartisan nature of our country.

Who are your two favorite world heroes? I hope you will indulge me if I include my father, Dennis Wasser; he is heroic. Also, Eleanor Roosevelt, who said, “The future belongs to those who believe in the beauty of their dreams.” What a badass!

What do you want written on your tombstone? She had a nice smile.
Personal Perspectives on Practicing Law in Other Countries

MANY NEW AND YOUNG U.S. LAWYERS aspire to practice in other countries but have no roadmap for how to realize that dream and no personal role models to follow. Insight from attorneys currently practicing internationally offers guidance on how to get started.

Language competence will inevitably play a role in which opportunities are available to an attorney. Similarly, an evaluation of acceptable cultural differences—e.g., an attorney’s willingness to live in a third-world country—may narrow the field of opportunities. However, with a grasp of those parameters, a new or young attorney can begin tackling the dream.

Aspiring international attorneys should decide whether they want to practice in a traditional setting, for example at a U.S. law firm that has offices in other countries, or with a government agency overseas or an international nonprofit. The decision will dictate many of the preparatory steps. Attorneys interested in public international law have a broad selection of locale given that many UN agencies and NGOs have offices around the world, including locations in Africa, Latin America, and Asia. On the other hand, for those looking to practice at a U.S. firm, international offices generally are located in big cities in Europe, the Middle East, and Asia.

Traditional Path
An attorney wishing to practice in a traditional law firm setting will likely be able to follow a traditional path—which is not to say the path will be easy. For example, Bora Rawcliffe, an attorney currently practicing at Skadden, Arps, Slate, Meagher & Flom LLP in London, recently transitioned from the Los Angeles office of Sheppard, Mullin, Richter & Hampton LLP.1 Her transition to London came to fruition after years of intense work focused on achieving that precise goal.

When Rawcliffe began practicing, she focused on obtaining a solid foundation in commercial litigation and white collar work, including internal investigations and the Foreign Corrupt Practices Act (FCPA).

“During my fourth year, and as a result of my focus on cross-border investigations work, I was offered the opportunity to move to London to advise European clients on a variety of matters involving U.S. laws including anti-corruption, sanctions, tax fraud, and anti-money laundering, and to represent them in enforcement actions brought by U.S. authorities such as the DOJ and SEC,” Rawcliffe said.

An attorney wishing to practice in a nontraditional setting will face hurdles unique to the nontraditional international law practice—not only in obtaining the first international position, but also in those that follow. Stephanie Montaño spent more than five years building her litigation skills in the United States before transitioning from her role as an attorney in the Los Angeles office of Venable LLP to a short-term role as a visiting attorney at the Institute for Human Rights and Business in Nairobi, Kenya.2

Looking back after eight months of working in Nairobi, Montaño said, “There tends to be a good deal of professional maneuvering that must be conducted during the transition process. This is because the vast majority of international legal positions are term-based roles, i.e., three months, six months, one year, etc. So the transition process requires a certain amount of stamina to think outside the box and not be deterred by the many unknowns and factors that are out of your control, while continuing to shape your career.”

The temporary nature of such positions affects certain logistical considerations, such as whether to keep a U.S. residence during the anticipated time away. Montaño kept her apartment.

Attorneys interested in practicing internationally, especially those whose U.S. practices do not readily transfer overseas, should begin working on international matters in settings outside their firms. For both Rawcliffe and Montaño, bar associations played a key role in the process. Joining international law committees and pursuing pro bono opportunities on international law matters allow aspiring international attorneys to work with senior attorneys who have practiced internationally—connections that can prove imperative to making the jump beyond the States.

Many nuanced factors affect the transition to international practice. Rawcliffe noted that for her transitioning took great patience, focus, and persistence. She encourages lawyers who wish to follow a similar path to learn as much as possible about the history and culture of the country of their destination, and to become familiar with the non-U.S. laws that will impact his or her practice in the new country.

A Foot in the Door
On moving to a less traditional practice of law, Montaño noted it can be difficult to get a foot in the door of the first non-law firm role. Thus, she recommends prioritizing paying off law school loans to enable flexibility in stepping away from the security of law firm life and accepting opportunities that continue to build a career in the desired direction, even if it means accepting short-term roles abroad.

Those aspiring to practice overseas should engage in the same practices recommended to most attorneys: sharpen legal skills, build strategic relationships,3 and stabilize their financial situations. After a few years of building a solid foundation, a new or young attorney should be poised for a successful practice internationally.

1 E-mail interview with attorney Bora Rawcliffe in London (Sept. 20, 2016).
2 Skadden covered Rawcliffe’s moving costs and residency and work permits—considerations an attorney otherwise would have to address on his or her own.
3 E-mail interviews with attorney Stephanie Montaño in Nairobi, Kenya (Oct. 13, 2016 and Oct. 31, 2016).
4 A good place to start might be joining LACBA’s International Law Section.

Victoria M. McLaughlin is an attorney with the Law Offices of William E. Crockett in Encino, California, where she practices business litigation. She is a member of the LACBA Barristers Executive Committee and has served as a volunteer attorney for Child Hope International in Port-au-Prince, Haiti.
Guidance on California's End of Life Option Act

AFTER A NUMBER OF DELAYS, California’s End of Life Option Act (the Act) became effective in June 2016. Only a few states have either legislatively or judicially approved an end of life or death with dignity option: Oregon, Washington, Vermont, Montana, and California. The Act is not without controversy. Some doctors believe it is a violation of the Hippocratic Oath, and many individuals and religious organizations oppose it. On the other hand, others believe in a right to choose to die in the event of terminal illness. Regardless of the views one may have on the morality of the Act, attorneys need to know how to advise clients on how it may be applied.

The Act provides a mechanism for a physician to prescribe a lethal dose of a drug to a qualified individual. The drug must be self-administered by the qualified individual; a physician may not assist. The Act uses the term “aid in dying drug,” defined as a drug that may be self-administered to bring about death. To qualify to receive the prescription the individual must be mentally competent or have the capacity to make medical decisions, defined as having the ability to “understand the nature and consequences of a health care decision, the ability to understand its significant benefits, risks, and alternatives, and the ability to make and communicate an informed decision to health care providers.”

The Act is based upon the individual’s ability to make and communicate an informed decision to health care providers. In this context, an “informed decision” is defined as one made by an individual with a terminal disease to request and obtain a prescription for a drug that may be self-administered to end the individual’s life. The decision can only be made after being informed of the relevant facts by the individual’s attending physician—the physician with primary responsibility for healthcare and treatment. The individual also must be diagnosed with a terminal disease and must voluntarily express his or her wish to receive the aid-in-dying prescription.

California Residency

The Act only applies to California residents. Residency in California for purposes of the Act can only be established through one of the following: 1) possession of a California driver’s license or other identification issued by the State of California, 2) registration to vote in California, 3) evidence that the person owns or leases property in California, or 4) filing of a California tax return for the most recent tax year. The California law is modeled after Oregon’s Death with Dignity Act (the Oregon Act), which recites the same four factors for establishing residency. However, California identifies the four factors as an exclusive list while Oregon permits other factors to be used as well.

A person who becomes a California resident must obtain a California driver’s license within 10 days. Residency is established for this purpose by voting in a California election, paying resident tuition, filing for a homeowner’s property tax exemption, or “any other privilege or benefit not normally extended to nonresidents.” As of July 1, 2016, and pursuant to AB 1465, an original (first-time) applicant for a driver’s license or identification card must present two acceptable documents as proof of California residency in addition to meeting all other existing driver license and identification card requirements. (See accompanying sidebar “Documents Acceptable as Proof of California Residency” on page 12 for a list of documents the state has approved to provide proof of California residency.) All residency documents must list the applicant’s first and last name, and the California residence address must match the residence address listed on the driver’s license application, with the exception of the last three items on the list.

The question of residency is most often raised when determining whether an individual is subject to California income tax. The California Revenue and Taxation Code defines a California “resident” as either an individual domiciled in California who is “outside the state for a temporary or transitory purpose” or every individual in the state for other than a temporary or transitory purpose. Residency and domicile have different legal meanings. In Estate of Glassford, a California court defined “domicile” as “the concurrence of physical presence in a particular place with the intention to make that place one’s home.” To change one’s domicile, a person must actually move to a new state with the intent to remain there permanently or indefinitely. Domicile is essentially the place in which one voluntarily establishes oneself and family, not for a limited or special purpose but with a present intention of making that place a time-fixed per-

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permanent home. Domicile is the place where, whenever absent, one intends to return.\textsuperscript{16}

The concept of domicile is relevant because lawyers often operate in the margins and gray areas seeking to push the boundaries for a client’s benefit. Domicile is a traditional concept in the definition of a California resident that lawyers consider or utilize in order to maximize a client’s benefit.

The question of residency may be important because people who have been diagnosed with a terminal illness may desire to move to California and establish domicile so that they may end their lives. Brittany Maynard’s story is illustrative. In 2014, Maynard was a terminally ill California resident unable to carry out her wish to die with dignity under California law. She was 29 years old, married, and suffering from brain cancer. Upon being advised that she might have to endure morphine-resistant pain, personality changes, and potential loss of verbal and cognitive abilities, Maynard, along with her husband and family, researched the treatment and prognosis.\textsuperscript{17} Eventually, she chose to die on her own terms, but California law did not permit her to carry out her decision. Maynard moved to Oregon, which did have a death with dignity law permitting her to die on her terms when the suffering became too great.\textsuperscript{18} She ended her life on November 1, 2014. California Governor Jerry Brown spoke to Maynard three days before her death and considered her family’s wishes and circumstances when deciding to sign the Act.\textsuperscript{19} However, future court decisions may bring new twists to long-standing concepts of California residency and domicile.

The Act seeks to simplify the complex definition of a California resident for the particular purpose of seeking relief under the Act. Time will tell as to how this will interact with California’s long-standing notions, laws, and precedents defining a California resident. The Act already interacts with existing law—for example, the requirement that a person becoming a California resident obtain a driver’s license within 10 days. This requirement would be based upon the traditional notions of when a person is a California resident. Obtaining a driver’s license is one of the means used to establish residency under the Act.

The Act requires that a qualified individual be a California resident. An understanding of the traditional notions of residency and domicile must be considered while viewing the four factors for establishing residency. For example, evidence that a person owns or leases property in California should be viewed in light of the concepts of domicile and residency. A person renting a hotel room for a night or two is not as persuasive as a person under a long-term lease.

If California courts are obliged to consider whether a person is domiciled in California and therefore meets the residency qualification, they may consider Oregon’s law, which has been in effect since 1997. In Oregon, a patient must be able to establish that he or she is currently a resident of Oregon, and here is no minimum requirement of previous residency. Similar to Oregon, California does not have a minimum requirement of previous residency.\textsuperscript{20}

A patient demonstrates residency by providing adequate documentation to the attending physician to verify that he or she is a current resident of Oregon. Factors demonstrating residency in Oregon include, but are not limited to: 1) possessing an Oregon driver’s license, 2) a lease agreement or property ownership document showing that the patient rents or owns property in Oregon, 3) possessing an Oregon voter registration, or 4) filing a recent Oregon tax return. The California Act and that of Oregon provide that owning or leasing property is a factor in establishing residency.\textsuperscript{21} There is no meaningful guidance on what constitutes leasing property within the meaning of the Act. The definition of a lease includes a rental.\textsuperscript{22} At first blush, renting a hotel room might satisfy the requirement for a lease. However, again, a short-term rental, such as a hotel room, would not appear to evidence establishing a domicile or residency. For residency, a stronger connection is required.

Under the Oregon statute, the attending physician is charged with the responsibility for determining whether the patient adequately established residency.\textsuperscript{23} The Act is silent as to who makes the residency determination. If California follows in Oregon’s footsteps, the attending physician would appear to have the authority to determine if the patient is a California resident for purposes of the Act. This may be problematic as a physician is...

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**Documents Acceptable as Proof of California Residency**

- Rental or lease agreement with the signature of the owner/landlord and the tenant/resident.
- Deed or title to residential real property.
- Mortgage bill.
- Home utility bills (including cellular phone).
- School documents including any document issued by a public or private primary, or secondary, or post-secondary institution, college, or university that either includes the applicant’s date of birth, or if a foreign school document, is sealed by the school and includes a photograph of the applicant at the age the record was issued.
- Medical documents.
- Employment documents.
- Faith based documents that include the name and address of the issuing organization.
- Insurance documents, including medical, dental, vision, life, home, rental, and vehicle.
- Internal Revenue Service or California Franchise Tax Board tax return.
- California Certificate of Title or Registration Card for a vehicle or Certificate of Ownership or Certificate of Number for a vessel.
- Change of Address Confirmation by the U.S. Postal Service (Form CNL 107).
- Documents issued by a U.S. government agency.
- Property tax bill or statement.
- Records from a financial institution.
- Voter registration confirmation letter or postcard issued by the California Secretary of State or a local California county elections officer.
- Proof of payment of resident tuition at a public institution of higher education located in California.
- An original copy of an approved Claim For Homeowners’ Property Tax Exemption (BOE-266) form filed with a local California County Assessor.
- Court documents that list the applicant as a resident of California.
- A letter on letterhead from a homeless shelter, shelter for abused women, nonprofit entity, faith based organization, employer, or government agency within the U.S. attesting that the applicant resides in California.
- A parent, legal guardian, or child may use a birth certificate and a spouse or domestic partner may use a marriage license or domestic partner registration certificate to trace his or her relationship to the individual to whom the two acceptable resident documents have been addressed.

Making Formal Requests

In addition to the residency requirement, an attorney should consider several other important issues when providing advice to a client. In particular, for example, California requires that the individual seeking to qualify for an end-of-life prescription must follow a procedure of formal request. The request cannot be made through a power of attorney, advance health care directive, conservator, healthcare agent, or any other legally recognized health care decision maker. An individual seeking assistance must make three personal requests directly to his or her attending physician. Two of the requests must be verbal and made at least 15 days apart. A separate written request must also be made to the attending physician. The physician must personally receive the requests and may not use a designee. Section 443.11 of the Health and Safety Code provides the form for the request. The request must be signed and dated in the presence of two witnesses. Only one of the witnesses may be related to the individual or own, operate, or be employed by the health care facility in which the individual resides or provides treatment, or be entitled to a portion of the person's estate upon death. The attending physician, consulting physician, or mental health specialist for the individual may not be a witness.

Each witness must indicate to the best of his or her knowledge and belief that 1) the individual is personally known or has provided proof of identity to the witness, 2) the request was voluntarily signed, and 3) the individual was under sound mind and not signing under duress, fraud, or under the influence. While the individual must be mentally competent to make the request, the request may be withdrawn at any time without regard to the individual's mental state. Mental capacity or competency is determined by the attending physician under the Act.

The written language of the request must be written in the same translated language as any conversations, consultations, or interpreted conversations or consultations between a patient and his or her attending or consulting physicians. The written request may be prepared in English even when the conversations or consultations or interpreted conversations or consultations were conducted in a language other than English if the English language form includes an attached interpreter's declaration that is signed under penalty of perjury.

If an interpreter is needed, he or she cannot be related to the qualified individual by blood, marriage, registered domestic partnership, adoption, or be entitled to a portion of the individual's estate upon death. In addition, the interpreter must meet the standards promulgated by the California Healthcare Interpreting Association or the National Council on Interpreting in Health Care or other standards deemed acceptable by the department for health care providers in California.

Assessing Legal Capacity

The attending physician must determine whether the individual has the legal capacity to make medical decisions. Before prescribing the patient, the attending physician must make a determination regarding whether the requesting adult has the capacity to make medical decisions. If there are indications of a mental disorder, the physician must refer the individual for a mental health specialist assessment. If a mental health specialist assessment referral is made, no aid-in-dying drugs may be prescribed until the mental health specialist determines that the individual has the capacity to make medical decisions and is not suffering from impaired judgment due to a mental disorder. The physician must also determine whether the requesting adult has a terminal disease and whether the requesting adult voluntarily made the request.
The attending physician must also confirm with the individual that he or she is making an informed decision by discussing whether the requesting adult is a qualified individual pursuant to subdivision o of Section 443.1 and confirming that the individual is making an informed decision by discussing with him or her all of the following: 1) the individual’s medical diagnosis and prognosis, 2) the potential risks associated with taking the drug to be prescribed, 3) the probable result of taking the drug to be prescribed, 4) the possibility that the individual may choose not to obtain the drug or may obtain the drug but may decide not to ingest it, and 5) the feasible alternatives or additional treatment opportunities, including, but not limited to, comfort care, hospice care, palliative care, and pain control.

The attending physician is also required to refer the individual to a consulting physician for medical confirmation of the diagnosis and prognosis, and for a determination that the individual has the capacity to make medical decisions and has complied with the Act’s other provisions. The attending physician must also confirm that the qualified individual’s request does not arise from coercion or undue influence by another person by discussing with the qualified individual, outside of the presence of any other persons, except for an interpreter as required pursuant to this part, whether or not the qualified individual is feeling coerced or unduly influenced by another person.

The individual also should understand and be advised by the attending physician of the importance of 1) having another person present when he or she ingests the aid-in-dying drug prescribed, 2) not ingesting the aid-in-dying drug in a public place, 3) notifying the next of kin of his or her request for an aid-in-dying drug (a qualified individual who declines or is unable to notify next of kin shall not have his or her request denied for that reason), 4) participating in a hospice program, and (5) maintaining the aid-in-dying drug in a safe and secure location until the time the qualified individual will ingest it.

The attending physician must also inform the individual that he or she may withdraw or rescind the request for an aid-in-dying drug at any time and in any manner. In addition, the physician must verify, immediately before writing the prescription for an aid-in-dying drug, that the qualified individual is making an informed decision. Once the physician has confirmed that all requirements are met and all appropriate steps are carried out in accordance with the Act, he or she must write a prescription for an aid-in-dying drug. The attending physician must refer the individual to a mental health specialist for an assessment if there are indications or symptoms of a mental disorder. The attending physician must confirm that the individual is making an informed decision and must discuss with him or her the medical condition risks associated with ingesting the aid-in-dying drug and the possibility of not using the drug after it is requested.

A second physician—the consulting physician—indispensable from the attending physician must confirm the diagnosis, prognosis, mental capacity of the individual, and all requirements of the Act. The consulting physician independently: 1) examines the individual and his or her relevant medical records; 2) confirms in writing the attending physician’s diagnosis and prognosis; 3) determines and reaffirms that the individual has the capacity to make medical decisions, is acting voluntarily, and has made an informed decision; (4) refers the individual for a mental health specialist assessment if there are indications of a mental disorder; 5) fulfills the record documentation required under Section 443.7; and (6) submits the compliance form to the attending physician.

Afterward, the attending physician must provide a final attestation form to the indi-
The individual must complete this form within 48 hours prior to self-administering the aid-in-dying drug. The individual is not required to inform his or her family of the decision.

The Act and Estate Plans
When working with terminally ill clients, trust and estate law attorneys should discuss the Act with clients and help them prepare for the process. The Act specifically precludes making a decision under the End of Life Option Act by means of a power of attorney, health care directive, or similar document. Also, the specific requirements of the Act for capacity and general compliance would seem to minimize the effectiveness of any such provision. For out-of-state clients, attorneys should consider including a provision in both powers of attorney and health care directives to authorize a change in the client’s domicile to be made by the agent. This will allow clients to change their domiciles more easily if necessary.

Changes in domicile may become increasingly important as the aging population increases. A change in domicile to a lower-cost and/or lower-tax state may reassure clients that they will not run out of money during their lifetimes. At least one court has held that a change in domicile may not be made on a power of attorney. The court determined that the concept of domicile is too personal to be made on a power of attorney as it relates to the individual’s subjective intent. Including the provision in the power of attorney for financial purposes, separate powers of attorney for personal care and the health care directive may minimize this argument.

2 Montana does not have a death with dignity statute, but the end of life option is legal in that state pursuant to a ruling by the Montana Supreme Court. Baxter v. Montana, 224 P.3d 1211 (2009).
3 Health & Safety Code §443.1(b).
4 Health & Safety Code §443.1(e).
5 Health & Safety Code §443.1(j).
6 Id.
7 Health & Safety Code §§443.2(a)(1), (2).
8 Health & Safety Code §§443.2(a)(3).
10 How to apply for a driver license if you are over 18, State of California Dept’ of Motor Vehicles, available at https://www.dmv.ca.gov/portal/dmv/detail/dl/dl_info (last visited Dec. 30, 2016).
11 California Residency Requirement for New Driver License (DL) and Identification Card (ID) Applicants, State of California Dept’ of Motor Vehicles, available at https://www.dmv.ca.gov (last visited Dec. 30, 2016). All documents acceptable as proof of California residency—of which two are required—are listed at this website.
12 Rev. & Tax. Code §17041(a).
13 Id.
15 Id.
18 Id.
20 Health & Safety Code §443.2(a)(3).
24 Health & Safety Code §443.3(a).
25 Health & Safety Code §443.3(c).
26 Health & Safety Code §§443.3(b)(3).
27 Health & Safety Code §443.4(a).
28 Health & Safety Code §443.1(e).
29 Health & Safety Code §§443.11(b)(1).
30 Health & Safety Code §§443.11(b)(3).
31 Health & Safety Code §443.5(a).
32 Health & Safety Code §§443.2-443.3.
33 Health & Safety Code §443.5(a)(3).
34 Health & Safety Code §443.5(a)(4).
35 Health & Safety Code §443.5(a)(5).
36 Health & Safety Code §443.6.
election year may have raised various contentious issues, local ballot initiatives in Los Angeles left voters with little choice but to confront the future of development in the city. Voters approved one development initiative in November and will vote on another in March. Both measures are symptomatic of the increasing tensions among groups that seek to maintain the status quo, groups frustrated by the increasing cost of living, and groups realizing the economic need for more development. Proponents of the initiatives may have felt compelled to intervene and change the current course of development, but the contents of the initiatives and their potential consequences illustrate the precarious task of asking the voters to balance complex policy choices through a single yes-no vote.

In November, voters approved ballot measure JJJ, the Build Better LA Initiative (BB-LA), which generally requires all projects with 10 or more residential units that need a general plan amendment or zone or height district change to include a certain percentage of affordable housing units. BB-LA also requires those projects to be constructed by contractors who meet certain labor requirements, which may increase wages and a project’s labor costs. In addition to BB-LA, Los Angeles voters will cast ballots in March on yet another development initiative aimed at constraining development in the city. The Neighborhood Integrity Initiative (NII), if approved, generally will impose a two-year building moratorium on projects that need to obtain an amendment to the general plan, zone change, or height district change to develop a more intensive use. The NII also would prohibit the city from approving amendments to its general plan solely for specific projects. Given the outdated nature of many elements in the city’s general plan and the community plans, NII could affect development in Los Angeles for decades.

**Backdrop**

Different planning and public policy dynamics in the city prompted supporters of the two initiatives to ask voters to confront these issues.
policy choices. Certain affordable housing advocates and unions championed the BB-LA initiative, citing the city’s lack of affordable housing options and need for more jobs with livable wages. As described in Section 2 of the BB-LA initiative findings, proponents were primarily concerned with the increasing homeless population in Los Angeles, the shortage of affordable housing, and the need to promote fair wages for local construction workers—problems they sought to address on the back of development projects that need a general plan amendment or zone change. These problems were summarized in an August 2015 study from the UCLA Luskin School of Public Affairs. The study reported that constraints on the housing supply across the city have led to an increase in home prices and rents while median income has not kept up with those increases. Indeed, voters approved the initiative by approximately 64 percent.

In contrast to BB-LA, advocates of the NII reacted to a broader systemic problem that has plagued planning in the city for years. According to city planners, Los Angeles has an outdated zoning code, and some elements in its general plan have not been updated in decades. The outdated planning regulations are inconsistent with how uses have evolved or become concentrated across different parts of the city. For example, many areas of the city, especially around new public transit opportunities, are not zoned for the density the city requires to accommodate its ever growing population. In addition, attempts to update the city’s zoning code or general plan have proven difficult since the updates require significant resources and rigorous review under the California Environmental Quality Act (CEQA). The update to the Hollywood Community Plan, for example, was invalidated by a trial court in 2014 for failing to comply with CEQA.

Against that backdrop, applicants have had few choices when seeking to construct projects with higher densities or mixed uses to align with the city’s evolution. Developers could seek a variance from existing zoning provisions, but variances may be hard to obtain and defend under the requirements of the Los Angeles Municipal Code (LAMC) and applicable case law. Alternatively, developers have pursued amendments to the general plan or a zone change to allow the desired density and use for a project. This option has led the city’s planning commission and the city council to approve general plan amendments or zone changes for individual projects. This practice has not necessarily led to poor planning but has nonetheless caused some communities to conclude that the city approves high density and new uses on a piecemeal basis without considering the concerns of the community at large.

The NII’s findings (Section 2) describe the state of development in the city as follows: “As a result of the city council’s approval of greater density and greater intensity of use through spot zoning and spot general plan amendments, there is a current and immediate threat to public health, safety and welfare.”

**Key Provisions of BB-LA and NII**

The heart of the BB-LA initiative is found in Section 5, which amends “appropriate sections” of the LAMC to add requirements for projects with 10 or more residential units that also require a general plan amendment or zone or height district change that permitted a more intense land use or an increase in allowable floor area, density, height, or will allow residential uses not previously allowed. Under the new requirements, these types of projects must include a certain percentage of affordable units, provide for affordable units off-site, or pay an in-lieu development fee. Those projects must also be constructed by contractors who: 1) are licensed and certified as required by the state and the city; 2) will make a good-faith effort to ensure that at least 30 percent of the workforce hours are performed by permanent residents of the city, including at least 10 percent whose primary place of residence is within a five-mile radius of the covered project; 3) pay their construction workers standard wages in the project area; and 4) employ 60 percent of their workforce from an apprenticeship training program or from workers who have on-the-job experience. In addition, Section 4 of the initiative amends Section 11.5.8 of the LAMC to divide Los Angeles into 37 planning areas and prevents an amendment to the general plan unless the city’s planning department completes a comprehensive assessment to ensure that such changes will not impact the availability of affordable housing or access to local jobs in the city.

The BB-LA initiative provides alternative compliance options for the on-site affordable housing requirements. Developers can construct affordable units off-site or acquire existing affordable units off-site and convert those units to a nonprofit community land trust and tenant ownership or both. Developers also may comply with the affordable housing requirements by paying an in-lieu development fee to the city. The city would establish the in-lieu fee by accounting for an “affordability gap,” which the city will establish by evaluating different market prices and affordability levels for different unit sizes. Section 5 further states that projects receiving a density bonus under the state’s affordable housing law or any other state or local program will not be eligible for a general plan amendment or zone change.

To focus development near transit centers, Section 6 of the BB-LA initiative instructs the city to develop a transit-oriented communities affordable housing incentive program (TOC) by amending Section 12.22 of the LAMC. This program applies to housing developments located within a one-half mile radius of a major transit stop, including existing transit stations and intersections with major bus routes. Within 90 days of enactment, Section 6 requires the director of planning to prepare the TOC Affordable Housing Incentive Program Guidelines, which will establish standards, incentives, and other necessary components for housing developments near transit centers to receive special incentives.

Section 4, the NII’s key provision, imposes a two-year moratorium that will prohibit the city’s approval of future entitlements and will bar the city from issuing building permits for certain entitlements that have already been approved. Specifically, the two-year moratorium will prohibit the city from approving a general plan amendment, zone change, or height district change, if any of those approvals would 1) change existing zoning to permit a more intense land use; 2) increase the floor area ratio, density, or height; or 3) lead to a net loss of land zoned open space, agricultural, or industrial. During the two-year moratorium, the initiative also prohibits the city from issuing a building or demolition permit for any project for which the city already granted a general plan amendment or a zone or height district change that resulted in 1) changes to existing zoning or height district that permitted a more intense land use or an increase in floor area ratio, density, or height from what was permitted in the current general plan; or 2) a change of zone from open space, agricultural, industrial, or any other type of zoning that is not open space, agricultural, or industrial.

The moratorium provides exceptions for 1) projects with 100 percent affordable units that seek a zone change or height district change (although the moratorium would apply to projects with 100 percent affordable units that still request a general plan amendment); 2) projects that require a building or demolition permit to repair, remove, or demolish unsafe or substandard conditions or to rebuild as a result of destruction by fire, earthquake, or other natural disaster; or 3) projects for which a vested right has accrued under state law or under the LAMC or to certain residential zones that are subject to an interim control ordinance.

Section 5 of the NII also changes the city’s authority to approve general plan amendments moving forward. Amending Section 11.5.6
of the LAMC, the NII prohibits the city from adopting a general plan amendment unless the amendment is for a geographic area that has a significant “social, economic or physical” identity. To be a geographic area with a significant social, economic, or physical identity, the geographic area must meet one of the following characteristics: 1) comprise an entire community or district plan area; 2) comprise an entire area that has been included in a specific plan; 3) comprise an entire named neighborhood council area; or 4) consist of an area at least 15 acres in size. The initiative expressly prohibits a general plan amendment for a single project or group of pending or concurrently submitted development projects. Also, the city council must accompany any general plan amendment with a specific finding that the amendment is not being approved solely to facilitate the approval of a pending project or projects.

Moving forward, the initiative amends Section 11.5.8 of the LAMC to require the city to adopt a schedule for the systematic public review and possible amendment of all elements of the general plan. The review and updating process is required to occur every five years, and the review program should include the review and possible updating of the city’s 35 community plans and port and air district plans. However, since voter initiatives cannot directly elect officials to adopt certain legislation in the future, NII acknowledges that updating the community plans is only “possible.”

In addition to changing the procedure for certain entitlements, the NII also restricts the city’s process for conducting environmental review of projects under CEQA. The initiative states an environmental impact report (EIR) under CEQA may only be prepared by the city or by a contract between the city and another public entity, not by the applicant or a consultant or third party retained by the applicant. Under current practice, project applicants can hire consultants directly and submit CEQA documents for the city’s review. The initiative also amends Section 12.21(y) of the LAMC to prohibit parking variances that would reduce the number of required on-site parking spaces by more than one-third of what is already required under the code.

Conflicts and Possible Legal Challenges

The courts may have to wrestle with what happens if voters approve the NII in addition to the BB-LA initiative, since the two measures may conflict. If faced with a potential conflict, courts must first try to reconcile the two initiatives to the furthest extent possible. However, some provisions may be irreconcilable. Potentially incompatible provisions include Section 5 of the NII, which prohibits the city from approving general plan amendments solely for specific projects, and Section 5 of BB-LA, which expressly allows the city to approve a general plan amendment for a specific project if that project complies with the affordable housing and labor requirements. The BB-LA initiative and NII include provisions stating that each respective initiative will prevail over the other if that initiative receives more votes than the other initiative. Notably, BB-LA will remain in full force for 10 years, unless amended or repealed by a vote of the people. The city council can reenact all or some of the BB-LA provisions without amendment following the expiration of the 10 years for two successive five-year periods. In contrast, the NII does not have a sunset provision. Instead, its terms can be amended or rescinded only by a vote in a future election.

Both initiatives may also contain defects that could be subject to legal challenge. First, voter initiatives are invalid at the time they are passed if they are inconsistent with the city’s general plan. The NII is potentially inconsistent with several of the polices in the city’s general plan, including policies related to growth, economic development, land use, housing, the reduction of air pollution emissions, and the promotion of mass transit. The NII may frustrate the achievement of those policies by preventing new projects from moving forward, and the NII makes no attempt to amend the general plan itself to address these inconsistencies.

The NII initiative may also be inconsistent with policies set forth in California’s planning and zoning law relating to the provision of housing throughout the state. This law requires each city or county to account for an appropriate share of the regional need for housing in a general plan. The NII will effectively limit the number of housing units that can be constructed throughout Los Angeles in the next two years and potentially long into the future.

The NII may also be invalid to the extent that it imposes an improper building moratorium not contemplated under the state’s planning and zoning law. The law allows cities to impose temporary moratoriums (not to exceed two years) on projects that may be “in conflict with a contemplated general plan, specific plan, or zoning proposal that the legislative body, planning commission, or the planning department is considering or studying or intends to study within a reasonable time.” Thus, building moratoriums usually accompany a city’s concurrent consideration of, or imminent plan to study, a potential change to the general plan or other applicable land use policy. Yet, no specific update to the general plan or a community plan has been proposed to the city that can be adopted within two years. Since the NII’s moratorium is not tied to any specific update to those plans, the initiative’s moratorium may be vulnerable in a legal challenge.

The BB-LA initiative may be invalid as a land use ordinance because all land use restrictions or regulations must bear a reasonable relationship to the public welfare, and absent that relationship, the initiative would be deemed to be arbitrary and discriminatory and an invalid exercise of police power. Proponents of BB-LA may face a significant challenge to show that the initiative’s labor requirements for residential projects bear a comparable reasonable relationship since arguably there is no connection between the labor requirements and the development of residential projects that require general plan amendments or zone changes.

Finally, Los Angeles is a charter city and its charter can only be amended in the same manner in which the charter was adopted in the first instance. By enacting an ordinance that affects the city’s authority to approve general plan amendments, the NII may be disguised as an indirect and impermissible city charter amendment.

Potential Policy Changes

Regardless of whether these legal challenges are pursued or are successful, the city has taken note of voters’ frustrations to address needed reforms in the planning process. Indeed, the city council is already considering multiple reform measures.

For example, to address affordable housing in Los Angeles, the planning department is evaluating a proposal to implement what is known as a “value capture” program. Under this program, the city will capture a public benefit in the form of affordable housing in exchange for granting entitlements that result in significant increases in the number of units allowed on a particular site for new residential and mixed-use projects. The city views the value capture program as something different from an incentive-based tool—for example, granting a density bonus for including affordable housing—since those tools are already priced into the value of land. In contrast, a general plan amendment or zone change that gives a benefit to a developer creates an increase in land value. Other cities have adopted value capture programs, including Boston, Chicago, Honolulu, New York, and San Francisco. Also, the city is exploring alternative options, including implementing a “linkage fee,” which would require new development to pay a fee toward affordable housing based on the size of the project.

To update its general plan, the city council is also considering a program to update the city’s 35 community plans over the next 10 years. Under the proposed program, the city would update three or
four community plans at a time, organized around three geographic regions: San Fernando Valley, Central/East and South/West/ Harbor. The city’s planning department is looking to create teams and hire new personnel across the three regions. The city is also considering a recommendation to amend the general plan in batches according to different geographic boundaries and may change its process to approve amendments for particular development projects. For example, the city would evaluate all proposed general plan amendments for the specified geographic areas during different months of the year. The city council is also considering recommendations to modify the process through which it reviews CEQA documents, including a recommendation that will require applicants to hire CEQA consultants from a prequalified list provided by the city to ensure quality and independence.

While the city and courts address these legal and policy issues, project applicants in Los Angeles that have started or will soon start the application process may be left in limbo because of unclear language in the initiatives. For example, the NII expressly covers out projects with vested rights as exempt from its provisions. Development rights become vested when a project has performed substantial work and incurred substantial liability in good faith reliance on a building permit. A vested right may also accrue if the city approves a vesting entitlement, such as a development agreement or vesting tentative tract map. Alternatively, under certain state laws, a “deemed complete” application may give rise to a vested right. Yet, proponents of the initiatives will surely challenge the use of these vesting mechanisms aimed at avoiding compliance with the initiatives.

Despite the reality that ballot initiatives may lead to unwanted consequences or even poor policy, cities in Southern California may face an increasing number of ballot initiatives concerning land use development if the voter malaise embodied in the two initiatives is not addressed through revised planning policies. Illustrating this potential trend, antidevelopment advocates in Santa Monica sponsored Measure LV on November’s ballot, otherwise known as the Land Use Voter Empowerment Initiative or LUVE Initiative. The LUVE Initiative generally would have required voters in Santa Monica to approve projects more than 32 feet in height, projects that have development agreements, or projects that require major amendments to Santa Monica’s planning policy documents in a special or general election. Santa Monica voters rejected the LUVE initiative by approximately 55 to 45 percent. Santa Monica’s rejection of the LUVE initiative may indicate that voters are not willing to adopt antidevelopment measures that might seriously hinder development. The LUVE results may forecast a similar rejection of the NII by Los Angeles voters in March. Yet voters’ approval of BB-LA in November shows that voters may be willing to approve development initiatives that seek to resolve a specific problem, such as the availability of affordable housing.

Balancing the competing concerns inherent in these complex policy issues is a difficult task for any legislative body. But trying to solve them, as BB-LA and NII try to do, through the initiative process can be fraught with peril. Striking the right balance between planning for future development and addressing concerns about continued growth is a complicated task that is difficult to address by a yes-no ballot measure. The initiatives put a burden on voters to balance difficult tradeoffs in arriving at a legislative consensus. Voters may not have sufficient information to weigh the important tradeoffs, and too few voters may turn out to vote in a municipal election. For example, turnout for Los Angeles’s municipal election in March 2015 was as low as 9 percent. Low turnout concentrates power to influence important planning decisions into the hands of a few. These types of ballot initiatives may lead to results that are contrary to what policymakers view as the best path forward for progress—for example, the results of the Brexit in the United Kingdom or voters’ rejection of the FARC peace deal in Colombia. Given the enormous task for cities to address concerns from all sides of the development debate, however, development initiatives and planning uncertainty may become more commonplace for voters and developers.


2 See Findings, BB-LA, supra note 1, §2; Findings, NII, supra note 1, §5.

3 See BB-LA, supra note 1, §5.

4 See NII, supra note 1.

5 California law requires that every city and county in the state adopt a comprehensive general plan to guide its future development. In the case of the City of Los Angeles there is a Citywide General Plan Framework Element that “establishes the broad overall policy and direction for the entire General Plan.” See General Plan, Dept. of City Planning, City of Los Angeles, available at http://planning.lacity.org (last visited Dec. 27, 2016) [hereinafter General Plan].

6 See NII, supra note 1, §4.
The JOBS Act of 2012 represents a sea change in the regulation of securities offerings. For the first time in U.S. history, companies may offer shares of stock to the general public without registering with the Securities and Exchange Commission (SEC). The most revolutionary aspect of the JOBS Act is Regulation CF, the new rule added to the Securities Act of 1933 that legalized equity crowdfunding. The JOBS Act’s two other new forms of public securities offerings, discussed elsewhere, are found in Rule 506(c) of Regulation D and in Regulation A.

Under Regulation CF, companies can sell up to $1 million-worth of shares of stock to anyone no matter the person’s net worth or income subject to certain limits on individual investment amounts. There is no SEC qualification requirement for securities offered through crowdfunding. This compares with offerings under Rule 506(c), which can raise an unlimited amount of capital without obtaining SEC qualification but can only be sold to accredited investors, and offerings under Regulation A, which are available to all investors but are limited to $50 million and must be qualified by the SEC.

President Barack Obama noted the significance of Regulation CF in his remarks during the April 5, 2012, bill-signing ceremony.

For start-ups and small businesses, this bill is a potential game changer. Right now, you can only turn to a limited group of investors—including banks and wealthy individuals—to get funding. A lot has changed in 80 years, and it’s time our laws did as well. Because of this bill, start-ups and small business will now have access to a big, new pool of potential investors—namely, the American people. For the first time, ordinary Americans will be able to go online and invest in entrepreneurs that they believe in.

Equity crowdfunding was born of Internet-based fund-raising campaigns that gained popularity with the success of two of the largest crowdfunding websites, Kickstarter and Indiegogo. Both offered a platform for crowdsourcing funding for projects that included films and environmental programs in exchange for t-shirts, movie production credits, or other tokens of appreciation. Prior to the JOBS Act, selling equity through crowdfunding—by definition a public offering—required SEC registration and blue-sky law qualification in each state in which the securities were offered. Regulation CF under Title III of the JOBS Act creates an exemption from registration specifically for equity crowdfunding and preempts state securities qualification laws.

Companies have raised just over $14 million using Regulation CF since it became effective in May 2016. In November 2016, Indiegogo announced its project backers would be able to make equity investments by using Regulation CF. Indiegogo is by far the largest crowdfunding platform to enter the equity space, having raised more than $1 billion from eight million backers of nonequity projects.
Entrepreneurs now may offer Indiegogo’s 15 million monthly visitors an opportunity to invest in their company.6 This entry by a major crowdfunding platform may kick-start the equity crowdfunding industry.

As the public capital markets have become accessible to all, general business lawyers, and not just securities law specialists, will need to respond to client questions about taking advantage of this new pool of potential investors. Thus, they require at least a working knowledge of the new methods and rules for raising capital under Regulations D, CF, and A under Titles II, III, and IV, respectively, of the JOBS Act. In particular, lawyers must be clear about the liabilities associated with these new offering methods, as the JOBS Act did not change the statutory joint and several civil liability for persons who control the company selling securities.

**Equity Crowdfunding**

The SEC’s rules for the new Regulation CF exemption enable entrepreneurs to raise up to $1 million during any 12-month period from anyone who wants to invest, subject to certain dollar limits on the amount of the individual investment. There is no requirement that the investor be accredited or sophisticated. If the investor’s net worth or income is below $100,000, the investor is subject to an investment cap of the greater of $2,000 or five percent of the lesser of the investor’s annual income or net worth. For those individuals whose net worth and annual income are at least $100,000, the investment cap is 10 percent of the lesser of the investor’s annual income or net worth, not to exceed an investment of $100,000.8 These caps reflect the aggregate amount an investor may invest in all offerings under Regulation CF in a 12-month period across all companies.9

To qualify for the crowdfunding exemption, the company must prepare an offering statement on Form C, which must include general information about the company and its officers, directors, and significant shareholders; the intended use of proceeds; the company’s ownership and capital structure; and financial statements for the two most recently completed fiscal years.10 If the offering amount is greater than $100,000 but less than $500,000, the financial statements must be reviewed by an independent accountant. If the offering amount is greater than $500,000, the financial statements must be audited, unless the company is conducting its first Regulation CF offering, in which case the financial statements need only be reviewed. For offerings less than $100,000, the financial statements need only be certified by the company’s principal officer.11

The company must file the offering statement with the SEC on Form C, but the filing is not reviewed by the agency.12 Once Form C is filed, the offering may commence immediately. The company is required to set forth a minimum or target offering amount, and investor proceeds must be deposited in a third-party escrow account until the minimum is reached.

A significant limitation under Regulation CF is the requirement that all offerings be conducted through a single Internet portal, which must either be registered with the SEC as a broker-dealer or as a new form of regulated entity—a funding portal. Funding portals are regulated by the self-regulatory organization, Financial Industry Regulatory Authority (FINRA). There are currently 21 funding portals registered with FINRA.13 Unlike broker-dealers, a funding portal may not offer investment advice or recommendations, solicit investments to buy the securities offered on its website or portal, pay commissions to its employees or agents, or take custody of investor funds. Similarly, unlike persons associated with a broker-dealer, persons associated with a funding portal are not subject to any licensing, testing, or qualification requirements.

Funding portals play a limited gatekeeper function.14 Regulation CF requires a funding portal to have a reasonable basis for believing that a company selling securities on its platform complies with Regulation CF.15 It is up to the portal to assess whether there is reason to question the reliability of a company’s representation of compliance.

As with any securities offerings, rules relating to permissible communications and advertising are critical to the success of the offering. Regulation CF strictly limits communications that mention the terms of the offering published by a company and third parties compensated by the company to promote its offering.16 Restrictions on advertising under Regulation CF raise difficult interpretive issues. How the SEC and courts resolve these questions will likely be informed by SEC staff positions articulated in future releases, no-action letters, and speeches.

**Advertising Offerings**

The new statutory exemption for equity crowdfunding provides that the company shall “not advertise the terms of the offering, except for notices which direct investors to the funding portal or broker.”17 The notices may not include anything other than: 1) a statement that the company is conducting an offering, the name of the intermediary through which the offering is being conducted and a link directing the investor to the intermediary’s platform; 2) the terms of the offering; and 3) factual information about the legal identity and business location of the company, limited to a brief description of the company.18 Historically, notices of this type have been referred to as tombstone advertisements, because the factual information about the company must be limited to a brief description of a few sentences. These restrictions on the content of advertising apply also to any third parties—for example, consultants and public relations firms—that the company compensates to promote the offering outside of the platform.19

The only other form of advertising expressly sanctioned by Regulation CF are company communications (identified as such) with investors and potential investors about the terms of the offering through communication channels provided by the intermediary on the intermediary’s platform.20 In adopting the crowdfunding rules, the SEC recognized the wisdom of the crowd—a central tenet of crowdfunding—and provided means for the company to respond to questions about the terms of the offering.21 To accommodate these rules, crowdfunding portals now universally include a comment section for each crowdfunding offering that allows the public and the company to post comments and responses.

The limited forms of advertising expressly authorized by Title III have been widely criticized, leading many to conclude that Title III is unworkable.22 Thus, there are now efforts to amend the JOBS Act.23 Advocates of reform argue that allowing companies to advertise “off portal” is essential to drive traffic to the portals where investors may view the terms of the offering and other requisite disclosures. If companies are not allowed to conduct their own campaigns to generate interest in their business and to direct prospective investors to the portal, few, if any, may know of the offering—a result surely not intended by lawmakers. Restricting off-portal communications further would prevent companies from taking advantage of modern communication technology and social media to drive traffic to the portal.

In May 2016, the SEC staff issued a number of compliance and disclosure interpretations that offer some relief from the strict statutory language.24 As to communications occurring outside the portal, the staff distinguishes between communications occurring before and after filing Form C. Prior to filing the offering statement on Form C, any activity that may constitute an offer is prohibited because Section 5 of the Securities Act prohibits offers as well as sales, unless registered or exempt from registration. The term “offer” is defined broadly in Section 2(a)(3) of the Securities Act as “every attempt or offer to dispose of, or solicitation of an offer to buy...for value.” The SEC and the courts interpret the term “offer” broadly. In adopting Regulation CF, the SEC staff explained that “the publication of inform-
Regulation CF has spawned new forms of investors. Securities solicitations heretofore never seen give rise to statutory rescission remedies to generally are referred to as “gun jumping” and prescribed. Violations of these restrictions generally are considered an effort to condition the market.

As to communications after Form C is filed, the SEC staff interprets the statutory prohibition on advertising the terms of the offering literally, and concludes that a company is not restricted in communicating information that might occur in the ordinary course of its operation as long as the communication does not refer to the terms of the offering. The SEC defines “terms of the offering” as the amount of securities offered, the nature of the securities, the price of the securities and the closing date of the offering period. Expanding on its interpretation, the SEC staff states that if a company’s advertisement does not include any of the terms of the offering, its message can extend beyond the limited information in the tombstone-type notices that include no more than the circumscribed company description. This suggests that the staff may allow companies and the third parties they hire to promote an offering to disseminate unrestricted information about the company in communications that direct prospective investors to the funding portal.

Before the JOBS Act, public offerings to unsophisticated investors required SEC registration or qualification. In registered public offerings, communications by the company and offering participants are strictly circumscribed. Violations of these restrictions generally are referred to as “gun jumping” and give rise to statutory rescission remedies to investors.

Although only effective since May 2016, Regulation CF has spawned new forms of securities solicitations heretofore never seen in the highly regulated public securities offering market. Incorporating the creativity of Madison Avenue (or its cyber equivalent), companies and their crowdfunding marketing consultants are crafting campaigns designed to appeal to unsophisticated investors. For example, two- or three-minute videos that rival Hollywood movie trailers are de rigueur. Promotional giveaways of t-shirts and other gifts, common in non-equity crowdfunding campaigns, are now featured in several crowdfunded securities offerings. For now, however, the SEC staff may monitor these new offering techniques and allow the new paradigm to unravel, at least until the next Bernard Madoff or Enron catalyst causes the regulatory pendulum to reverse course. It is likely, though, that before the regulators take action the crowd will lose money, as early-stage investments in startups are risky.

Prior to the JOBS Act, issuers engaged financial intermediaries—e.g., investment banking firms—to sell their securities to the public. The JOBS Act’s disintermediation of Wall Street has left it to the companies themselves to underwrite their offerings and has spawned a cottage industry of crowdfunding consultants and finders who assist companies with selling their securities. The emergence of this new category of consultants is bringing to bear difficult securities-law issues in equity crowdfunding offerings, namely, the permissible scope of activity of consultants and finders who are not registered and licensed as broker-dealers and the compensation that issuers may pay them. The question is whether these consultants and finders are required to be registered and licensed, and, if they are not, whether issuers will be allowed to pay “transaction-based compensation,” i.e., commissions or other compensation contingent on the sale of a security to consultants who assist issuers in finding and soliciting investors.

Federal securities laws and state blue-sky laws prohibit a person from “engaging in the business of effecting transactions in securities” without being first registered with the SEC as a broker-dealer and licensed with FINRA. Section 15 of the Securities Exchange Act of 1934 requires that brokers and dealers in securities register with the SEC. Each state also has its own requirements for broker/dealer registration. A “broker” is “any person engaged in the business of buying and selling securities for his own account, through a broker or otherwise.” Many unlicensed consultants and finders work for transaction-based compensation by erroneously relying on an old, narrow SEC staff policy exception—the so-called “finder’s exception”—to the broker-dealer licensure requirement. For many years, knowingly or not, unregistered finders relied on a series of SEC staff no-action letters, including one in particular, in which the staff in 1991 agreed that...
it would not take enforcement action against entertainer Paul Anka for receiving a transaction-based fee for introducing an investment opportunity to persons whom he believed to be accredited investors. The staff recognized that the transaction was a one-time occurrence for Anka and that he was not in the business of providing finder services. The SEC’s interpretation at that time was predicated on the absence of the following factors, all of which tend to indicate broker/dealer activity: participation in negotiations, counseling investors on the merits of investing, recommending the investment to investors, receiving compensation based on a percentage of the offering proceeds, holding securities or cash, providing details of the financing to investors, and conducting sales efforts.

**Unregistered Finders**

Many unregistered finders, some of whom labeled themselves as “investment bankers,” ignored, or were unaware of, the primary factor in the SEC’s decision that the compensation was a one-time occurrence. As a result, in 2010, the SEC staff issued a no-action letter in which it declared that the receipt of transaction-based compensation alone, which the SEC staff often describes as a “salesman’s stake,” may be sufficient to require licensure. In the letter, SEC staff recounted how the law firm of Brumberg, Mackey & Wall, P.L.C., itself sought to receive a finder’s fee for introducing its client to potential investors. The law firm represented to the SEC staff that it would not engage in any negotiations whatsoever on behalf of its client, would not provide any potential investor with information about the client that might be used as the basis for negotiations for funding, and would not have responsibility for, nor make recommendations concerning, the terms, conditions, or provisions of the financing. According to the SEC staff, “a person’s receipt of transaction-based compensation in connection with these activities is a hallmark of broker-dealer activity.” One federal district court has rejected the SEC staff’s interpretation of the law.

As with the finder’s exception, unlicensed persons sometimes mistakenly rely on the “issuer exemption” from broker registration under Securities Exchange Act Rule 3a4-1. That rule provides a nonexclusive safe harbor from broker-dealer registration for an individual employee or agent of the issuer who, among other things, “is not compensated by the payment of commissions or other remuneration based either directly or indirectly on transaction in securities.” Whether a particular compensation arrangement is “other remuneration” based either directly or indirectly on transactions in securities depends on the particular facts and circumstances. For example, in determining whether a particular compensation arrangement involving the payment of bonuses would not be permissible under the rule, the following factors may be relevant: 1) when the offering commences and concludes, 2) when the bonus is paid, 3) when it is determined that a bonus will be paid, 4) when associated persons are informed of the issuer’s intention to pay a bonus, and 5) whether the bonus paid to particular associated persons varies with their success in selling the issuer’s securities. Issuers sometimes view paying transaction-based compensation to unlicensed consultants and finders as the unlicensed person’s problem. Indeed, some issuers sometimes use the person’s unlicensed status as a basis to void the person’s compensation arrangement. However, paying an unlicensed broker to solicit investors exposes an issuer to potential significant civil liability, as there is authority for investors to seek rescission against such an issuer.

At the federal level, Section 29(b) of the Securities Exchange Act of 1934 provides that “[a]ny contract made in violation of any provision of this title … shall be void.” Many consider this language sufficiently broad to support a rescission claim against an issuer who pays transaction-based compensation to an unlicensed broker-dealer. A number of appellate courts have interpreted Section 29(b) to allow rescission by investors and by issuers of transactions in securities with unregistered broker-dealers. While the holdings of these cases invalidated the agreement and transaction between the investor or the issuer and the nonregistered finder, there is dicta in at least one case that the offering itself, as evidenced by the contract between the issuer and the investor, also could be invalidated by Section 29(b).

In California, Section 25501.5 of the Corporations Code provides a right of rescission to investors who purchase a security from an unlicensed broker-dealer. Section 1029.8 of the Civil Code makes mandatory treble damages (up to $10,000) against a person who causes injury or damage to another person as a result of providing goods or performing services for which a license is required by specified statutes. It further provides that the court “may, in its discretion, award all costs and attorney’s fees to the injured person if that person prevails in the action.” The California legislature amended Section 1029.8 to make specific reference to the broker-dealer and investment adviser registration provisions when it enacted Corporations Code Section 25501.5.

To facilitate capital access, the California legislature enacted a new law that took effect in January 2016, which attempts to offer some relief for finders in transactions exclusively within California. However, the new California law does not include any relief for solicitors who provide any more than the most basic information about the issuer and offering. The law also requires that the finder file an information statement with the California Department of Business Oversight prior to the transaction. Moreover, the law does not provide relief from the SEC’s strict interpretive position or from every other state’s broker-dealer registration requirements.

Lawyers are not immune from federal and state broker-dealer registration requirements. Last year the SEC sued several lawyers and law firms, including one Los Angeles immigration law firm, for acting as unregistered brokers. The law firms accepted commissions in connection with investments made as part of the federal EB-5 Immigrant Investor Program. An SEC press release quoted Andrew J. Ceresney, director of the SEC’s Division of Enforcement: “Individuals and entities performing certain services and receiving commissions must be registered to legally operate as securities brokers if they’re raising money for EB-5 projects…[the] lawyers in these cases allegedly received commissions for selling, recommending, and facilitating EB-5 investments, and they are being held accountable for disregarding the relevant securities laws and regulations.”

**Liabilities**

The JOBS Act opened the door to nonaccredited investors who want to participate in the world of investing in unregistered securities offerings. Prior to the JOBS Act, although Regulation D and most states allowed companies to accept investments from up to 35 nonaccredited investors, securities lawyers frequently counseled clients to steer clear of this investor class. The disclosure requirements for nonaccredited investors were nearly identical to those required in a registered public offering. And the risk of a liability claim by an unsophisticated investor outweighed any benefit of receiving the relatively small investments.

Lawyers counseling clients who undertake exempt public offerings in the new paradigm under the JOBS Act must appreciate the greater exposure to liability—to their clients and to themselves. Courts and the SEC have long considered securities lawyers as occupying a unique role in advising companies selling securities to the public. Both the SEC, in its civil enforcement actions, and the U.S. Department of Justice, which prosecutes criminal securities cases, have sued lawyers and routinely remind the public of attorneys’ gatekeeping function. Exposure to securities laws claims is heightened in equity crowdfunding offerings in which there is typically no involvement of a professional intermediary, including an investment banking firm, which,
The Los Angeles County Bar Association certifies that this activity has been approved for Minimum Continuing Legal Education credit by the State Bar of California in the amount of 1 hour. You may take tests from back issues online at http://www.lacba.org/mclesselftests.

MCLE Test 265 is based on parts 1 and 2 of the article “Ready Capital,” on the JOBS Act. See Los Angeles Lawyer December 2016 and February 2017 respectively.

1. An individual accredited investor must have an annual income of $200,000 in each of the two most recent years (or $300,000 joint income) and have a net worth in excess of $1 million, excluding home equity.
   True.
   False.

2. There is no limit on the amount of securities that may be sold in an offering pursuant to Rule 506 of Regulation D.
   True.
   False.

3. A company may not sell securities to a nonaccredited investor pursuant to Rule 506(b) of Regulation D.
   True.
   False.

4. Today, 99 percent of all private offerings under Regulation D are conducted pursuant to Rule 506.
   True.
   False.

5. Securities offerings pursuant to Regulation A preempt state securities “blue sky” laws.
   True.
   False.

6. Investors in securities offerings pursuant to Regulation CF and Regulation A are not required to satisfy any sophistication test.
   True.
   False.

7. Companies that conduct securities offerings under Tier 1 of Regulation A are subject to ongoing reporting requirements.
   True.
   False.

8. Equity crowdfunding offerings under Regulation CF (Title III of the JOBS Act) must be conducted using a funding portal regulated by the Financial Industry Regulatory Authority (FINRA).
   True.
   False.

9. There is no requirement that an investor in an equity crowdfunding offering under Regulation CF be accredited or sophisticated.
   True.
   False.

10. If either an investor’s annual income or net worth is $5 million or more, there is no limit on the amount that the investor may invest in all crowdfunding offerings under Regulation CF in a 12-month period.
    True.
    False.

11. An issuer of securities in a crowdfunding offering under Regulation CF must file with the SEC an offering disclosure statement on Form C.
    True.
    False.

12. A securities offering under Regulation CF may not commence until the SEC qualifies the Form C.
    True.
    False.

13. There are no restrictions on communications or advertising securities offerings under Regulation CF.
    True.
    False.

14. Before the JOBS Act, public offerings to unsophisticated investors required SEC registration or qualification.
    True.
    False.

15. The so-called “finder’s exception” to broker-dealer licensure requirements allows an unlicensed person to receive transaction-based compensation in connection with the sale of a security, provided that the unlicensed finder does not negotiate the terms of the investment.
    True.
    False.

16. Under the “issuer exemption” safe harbor Rule 3a4-1 an employee who engages in the sale of the employer’s securities may receive a cash performance bonus based on the amount of securities sold.
    True.
    False.

17. Paying an unlicensed broker to solicit investors exposes an issuer to potential significant civil liability.
    True.
    False.

18. The investor plaintiff bears the burden of proof to establish that the company defendant violated the requirements of the exemption from registration.
    True.
    False.

19. Failure to satisfy the requirements of Rule 506(c), Regulation A or Regulation CF will result in loss of the exemption from registration and give rise to liability under Section 12(a)(5) only if the investor plaintiff proves that the company defendant acted with scienter or negligently.
    True.
    False.

20. In California, attorneys rendering securities law advice are held to a higher standard of care in legal malpractice actions.
    True.
    False.

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Mark your answers to the test by checking the appropriate boxes below. Each question has only one answer.

1. □ True □ False
2. □ True □ False
3. □ True □ False
4. □ True □ False
5. □ True □ False
6. □ True □ False
7. □ True □ False
8. □ True □ False
9. □ True □ False
10. □ True □ False
11. □ True □ False
12. □ True □ False
13. □ True □ False
14. □ True □ False
15. □ True □ False
16. □ True □ False
17. □ True □ False
18. □ True □ False
19. □ True □ False
20. □ True □ False
as a registered broker-dealer, is required to conduct due diligence investigations in connection with the securities offering. In most equity crowdfunding offerings, third-party due diligence is left to the lawyers and accountants, who often end up as the only deep-pocket defendants when investors sue to recover their losses.

Liability under federal and state securities laws is unlike liability under the common law. Federal and state statutory securities law remedies offer both procedural and substantive benefits to investors unavailable to them under rights of action at common law and in equity for breach of contract, breach of warranty, and the tort remedy for common law deceit. The purpose of the civil liability provisions of California’s Corporate Securities Law of 1968 “is to create statutory liability that eliminates some of the elements of common law fraud, but balances this expansion of liability by placing other restrictions on recovery.” The statutory securities rescission remedies sometimes may be described as providing for strict liability because unless the defendant company is able to sustain affirmative burdens of proof, it will be liable. More important, in the wake of the 1929 stock market crash and Great Depression, Congress and the states imposed joint and several rescission liability on the individuals who control the company that violates the securities laws, unless the control person is able to sustain the burden of a due diligence affirmative defense.

Two Bases

Section 12(a) of the Securities Act provides investors with two bases to assert a right of rescission. Under Section 12(a)(1) investors have a right of rescission against any person who offers or sells a security in violation of the registration requirement. Thus, failure to satisfy the requirements of rule 506(c), Regulation A or Regulation CF will result in loss of the exemption from registration and give rise to liability under Section 12(a)(1). It imposes almost absolute liability when the seller is unable to prove that it satisfied the requirements of the exemption. The plaintiff is not required to prove scienter or even negligence by a company defendant that fails to establish the requirements of the applicable exemption.

The second basis for rescission is pursuant to Section 12(a)(2), which provides investors a right of rescission against sellers who offer or sell securities by means of a prospectus or oral communication that contains misstatements and omissions of material information. However, unlike Section 12(a)(1), Section 12(a)(2) provides a due diligence affirmative defense that the seller “did not know, and in exercise of reasonable care could not have known, of such untruth or omission.” Hence, counsel must assist management in memorializing its reasonable basis for the statements made in its offering document. Section 12(a)(2) claims also are subject to a “loss causation” affirmative defense that the investor’s loss was not caused by the false or misleading statement or material omission.

In California, Corporations Code Sections 25501 and 25503 provide a remedy similar to the federal remedies under Securities Act Sections 12(a)(1) and 12(a)(2). Similarly, California provides for joint and several liability of individuals who control the company. California’s joint and several control person liability provision, Corporations Code Section 25504, is especially broad, providing that every person who directly or indirectly controls a company liable under Section 25501 or 25503, every partner in a firm so liable, every principal executive officer or director of a corporation so liable, every person occupying a similar status or performing similar functions, every employee of a company so liable who materially aids in the act or transaction constituting the violation, are also liable jointly and severally liable with and to the same extent as such company, unless the other person who so liable had no knowledge of or reason to know of the untrue or misleading statement or material omission. In California, the corporate issuance of unqualified securities regardless of whether they participated in the transactions at issue, or controlled the company. The court rejected outright the outside directors’ claim that the “weight of authority” supported their argument that the plaintiffs had to plead facts to show that the outside directors controlled the company.

Lawyers counseling clients who undertake exempt offerings in reliance on Rule 506(c) of Regulation D, Regulation A, or Regulation CF must appreciate the greater exposure to liability in offerings made to the public. In California, attorneys rendering securities advice are held to a higher standard of care in legal malpractice actions. Representing a company conducting an exempt offering subjects the lawyer to the SEC rules governing standards of professional conduct of lawyers. Equity crowdfunding offerings present unique challenges for lawyers who engage in general business practices as well as securities law. The absence of professional intermediaries in crowdfunding offerings, in addition to sometimes leaving lawyers and accountants as the only deep-pocket defendants, assigns due diligence responsibilities to the company and its counsel. Establishing evidence of the requisite due diligence is paramount to protecting the company and its control persons because if the affirmative burden of the due diligence defense when it is available is not sustained, liability to investors is nearly absolute.

In determining if attorneys have performed adequate due diligence, California practitioners should be aware of the Ninth Circuit decision in FDIC v. O’Melveny & Myers, in which the Federal Deposit Insurance Corporation (FDIC), as receiver for failed savings and loan association American Diversified Savings Bank (ADSB), filed a lawsuit in the Central District of California against O’Melveny & Myers claiming professional negligence in connection with its legal advice in counseling ADSB in private securities offerings. O’Melveny prepared two private placement memoranda and wrote substantial portions of the memoranda, edited other portions, and performed a due diligence review. It was undisputed that the memorandum contained false information about the company’s financial condition. The FDIC commenced its suit against O’Melveny, charging the firm with professional negligence, negligent misrepresentation, and breach of fiduciary duty. In reversing the trial court’s summary judgment in favor of O’Melveny, the Ninth Circuit stated:

Part and parcel of effectively protecting a client, and thus discharging the attorney’s duty of care, is to protect the client from the liability which may flow from promulgating a false or misleading offering to investors. An important duty of securities counsel is to make a “reasonable, independent investigation to detect and correct false or misleading materials.” This is what is meant by a due diligence investigation.

The O’Melveny decision has been cited for the proposition that the duty of care
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owed by an attorney to a client includes reasonably protecting the client from liability that might flow based on its agent’s dissemination of false or misleading statements to the public.64

Under the restrictive securities laws in effect for the 90 years prior to the JOBS Act, entrepreneurs who did not have access to friends and family who could provide seed capital had little chance of getting their startups off the ground. Today, seed funding at the attainable $250,000 to $750,000 level—not the millions of the past—could, with modern technology, be just enough to advance an entrepreneur’s ideas, develop a prototype, enter into a first contract, or otherwise validate a vision or business model in order to get on the radar of institutional investors and rise to the next level of success. Without such early funding, those entrepreneurial businesses would be lost in a sea of concepts floating over the transom to the inboxes of managers at venture capital funds. Thus, in theory, Regulation CF enables anyone to reach out to capital sources and raise seed levels of money. No doubt, without the benefit of professional financial intermediaries, such as investment bankers, entrepreneurs on their own will face challenges raising capital. What the JOBS Act offers, however, is a pathway for companies eventually to reach these public equity markets, which prior to the JOBS Act, were accessible to only the most privileged few. It will be up to business lawyers to navigate the new securities rules and regulations to ensure that their clients do not get lost along the way.

“Fasten your seat belts, it’s going to be a bumpy night.”65


8 17 C.F.R. §227.100.

9 Securities issued in offerings under Regulation CF are exempt from the registration requirement of Section
MICHAEL CALLAWAY

Securities and Exchange Commission’s (SEC) practice of initiating administrative proceedings against defendants to be adjudicated by the SEC’s in-house administrative law judges (ALJs) has taken place since the 1940s. Presently, five ALJs oversee the SEC’s Administrative Law Court. All are appointed by the SEC’s Office of Administrative Judges.

In the past few years, the SEC has dramatically increased the percentage of cases it has filed as administrative proceedings as opposed to actions in the federal courts. The SEC enjoys a much higher success rate in such proceedings compared with those overseen by an independent federal judiciary. A study by the Wall Street Journal demonstrated that the SEC’s success rate in administrative proceedings from October 2010 through March 2015 was 90 percent compared with its 69 percent success rate in federal actions over the same period. The study also showed that when defendants who received an adverse ruling from an ALJ appealed directly to the SEC, 95 percent of such appeals were resolved in favor of the SEC.1

The SEC has acknowledged that it has filed more ALJ proceedings in the recent past than previously and has contended that such increases are due to changes under the Dodd–Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank) that permitted the SEC to seek certain penalties in ALJ proceedings that it previously could only seek in actions filed in federal court.2

Criticism against the SEC’s paradigm shift has been levelled from many quarters, including from one federal judge.3 Critics contend that the administrative arena lacks many of the due process protections of the federal courts, including an independently appointed judiciary, the opportunity for extensive discovery, and juries. Because the mere levying of claims by the SEC may result in devastating consequences for defendants and their families—e.g., the loss of jobs, careers, and income—critics argue that the process should be more fair and impartial. Indeed, the administrative process is held to be unfair to defendants who are judged first by an ALJ appointed by and beholden to the SEC and again on an appeal to the SEC’s commissioners. Various commentators have said that a system in which the hand of the SEC is so heavy in administrative proceedings—from determining whether or not to institute proceedings to selecting the ALJ deciding the outcome to

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determining on appeal whether or not an adverse judgment should be affirmed or reversed—is counter to the values of fairness and integrity inherent in the American judicial system. They also have contended that the selection of ALJs by the SEC’s Office of Administrative Law judges rather than by the president violates the Appointments Clause of the U.S. Constitution.

Public Criticism

This public criticism and media attention has resulted in two rounds of judicial challenges to the SEC’s administrative proceedings. Round one concerned the threshold issue of when such a challenge could be mounted—before the ALJ process had concluded or at the end of that process. This round largely appears to be over. All circuit courts of appeals that have considered the issue have found that these challenges must wait until the ALJ process has run its course. Round two addressing substantive arguments about the constitutionality of the SEC’s ALJ process is just beginning. Already, a circuit split has developed on issues that could lead to review by the U.S. Supreme Court. If the Supreme Court ultimately decides that the SEC’s ALJs presided over administrative proceedings in violation of the Appointments Clause of the U.S. Constitution, thousands of ALJ awards over many years in contested hearings potentially may be invalidated.

In response to criticism that its court system lacks due process, the SEC proactively changed and proposed changes to some of its administrative proceedings rules. However, these changes are not sufficient to rebut critics’ concerns because they do not address the fundamental unfairness of proceedings prosecuted and adjudicated by individuals employed by the same agency.

Finally, several legislative movements have been initiated by Republican members of the U.S. House of Representatives to address some of the concerns. It is unclear what impact a Republican in the White House will have on these efforts; however, President Donald Trump supports repeal of Dodd-Frank. If Dodd-Frank is repealed, the SEC may be forced to proceed in federal court if it wishes to pursue certain penalties that will no longer be available in administrative proceedings. Also, President Trump may support the legislative efforts of Republican Congressman Jeb Hensarling of Texas to repeal and replace certain portions of Dodd-Frank, including a specific proposal to permit all defendants in ALJ proceedings to remove such cases to the federal courts. If such legislation were passed, most defendants likely would choose removal to the federal courts resulting in a dramatic reduction of ALJ proceedings. Before round two in the courts has concluded, it is possible that legislative efforts may put an end to this issue and curtail or significantly reduce the SEC’s ability to bring cases in an administrative forum.

In 2014, defendants in SEC administrative proceedings began filing suits in federal courts to enjoin ALJ proceedings before they had run their course. The defendants contended that such proceedings were unconstitutional because the ALJs were appointed in violation of the Appointments Clause. District courts initially reached different conclusions about whether or not they had jurisdiction to reach the merits of the constitutional challenges made to an administrative proceeding under the three-prong test outlined in *Thunder Basin Coal Company v. Reich.* Some courts found that they had jurisdiction to consider the merits, while others held that they did not.

In the wake of these conflicting lower court rulings, appeals were taken. The Second, Fourth, Seventh, Eleventh and District of Columbia circuit courts of appeals have held they lack jurisdiction to entertain constitutional challenges to ALJ proceedings until such proceedings have run their course. No circuit court of appeals has disagreed.

Accordingly, the first round of litigation challenges to the SEC’s administrative proceedings is over. Five circuit courts of appeals concurred that the lower courts have no jurisdiction to consider constitutional challenges to the ALJ process until after the exhaustion of all administrative remedies. As a result, the U.S. Supreme Court will not take an interest in this issue unless another circuit court of appeals takes a different tack and creates a circuit split.

Constitutional Challenges

Round one simply delayed the day of reckoning for courts to reach the merits. On August 9, 2016, the District of Columbia Circuit Court of Appeals became the first appellate court to do so.

In *Lucia Companies, Inc. v. SEC,* defendants received an adverse ruling in an administrative proceeding and exhausted all appeals to the SEC. On appeal, the commission found the defendants committed antifraud violations and imposed the same sanctions as the ALJ. The commission also rejected the defendants’ argument that the administrative proceeding was unconstitutional because the ALJ was not appointed in conformity with the Appointments Clause. Although the parties conceded that the president does not appoint ALJs, the commission found that its ALJs are employees and not officers and, therefore, the Appointments Clause does not govern.

The *Lucia* defendants filed a petition for review to the District of Columbia Circuit Court of Appeals and renewed the argument concerning the Appointments Clause. The Lucia court’s analysis focused on whether or not ALJs were officers subject to the Appointments Clause or employees who are not subject to the Appointments Clause. The court’s analysis “begins, and ends” with a consideration of whether or not ALJs issue “final decisions of the Commission.” If ALJs do not issue “final decisions of the Commission,” they are employees who are not subject to the Appointments Clause.

In their briefs to the court, the defendant petitioners noted that an ALJ decision “becomes the final word of the agency unless further review is granted” and thus “[t]he ALJ’s decision is not replaced by a final agency order, the ALJ decision itself ‘become[s] final.’” In other words, unappealed ALJ decisions automatically become the final action of the commission. Accordingly, the petitioners argued that ALJs do issue final decisions of the commission and therefore are officers subject to the Appointments Clause. They also noted that “ALJ’s rulings are in fact rarely disturbed” and that the ALJ involved in the underlying matter “has apparently never been reversed by the SEC in more than 50 cases.”

The Lucia court, however, was not persuaded. It held that “[t]he Commission’s final action is either in the form of a new decision after de novo review or, by declining to grant or order review, its embrace of the ALJ’s initial decision as its own.” It further held that “the Commission’s ALJs neither have been delegated sovereign authority to act independently of the Commission nor, by other means established by Congress, do they have the power to bind third parties, or the government itself, for the public benefit.” Notwithstanding the evidence in the petitioners’ brief that ALJ decisions are rarely disturbed by the commission, the court held that the “petitioners offer neither reason to understand the finality order to be merely a rubber stamp, nor evidence that initial decisions of which the Commission does not order full review receive no substantive consideration as part of this process.”

On December 27, 2016, in *Bandimere v. SEC,* the Tenth Circuit Court of Appeals issued a ruling directly contrary to Lucia. The court held that the SEC ALJ who presided over an administrative proceeding was an inferior officer who held his office in violation of the Appointments Clause.

The Bandimere court disagreed with the Lucia court’s creation of a litmus test to determine whether or not the Appointments Clause had been violated, that is, whether the SEC ALJs’ lack of final decision-making authority automatically means that the ALJs were not subject to the Appointments Clause. Instead, the Tenth Circuit held that such a conclusion should hinge on the ALJs’ duties and not on final decision-making power.
In so doing, the court held that “[w]hether SEC ALJs can enter final decisions is not dispositive to our holding” but “the SEC’s argument that its ALJs can never enter final decisions is not airtight.” The court noted that the SEC may decline to review an ALJ decision or enter an order stating that the ALJ’s initial decision is final without engaging in review and that in fact 90 percent of all initial SEC ALJ decisions follow such “a path for an initial decision to become final without plenary agency review.” The court recognized that SEC ALJ duties are more than ministerial tasks and that the ALJs carry out important functions pursuant to the laws of the United States. The SEC’s power to review its ALJs does not transform them into lesser functionaries, the court said. Rather, it shows the ALJs are inferior officers subordinate to the SEC Commissioners. Since the SEC ALJ held his office unconstitutionally when presiding over the underlying administrative proceeding, the Court granted the petition for review and set aside the SEC’s opinion.

In *Bandimere*, a vigorous dissent by Judge McKay relies on *Lucia* to contend that SEC ALJs are not inferior officers and thus not subject to the Appointments Clause because they cannot enter final decisions. The dissenting opinion also contends that the majority’s holding is “quite sweeping, and I worry that it has effectively rendered invalid thousands of administrative actions.” Judge Briscoe’s separate concurring opinion refutes the contention that the ruling potentially invalidates all ALJs, and not simply SEC ALJs. Judge Briscoe also criticizes the dissent’s reliance on *Lucia’s* reasoning and repeats the conclusion of the majority that whether or not an ALJ possesses “final decision-making authority” is not the “*sine qua non* of inferior Officer status.”

In the immediate future, the SEC doubtless will seek a rehearing in *en banc* *Bandimere*. If that effort and the pending request for a rehearing in *en banc* *Lucia* are unsuccessful, then this issue is on track for review by the U.S. Supreme Court to resolve the split between the Tenth and District of Columbia circuit courts of appeals. Other circuit courts of appeals also will weigh in on this issue and choose to follow either *Lucia* or *Bandimere*. If the *Bandimere* decision holds through all appeals, the SEC potentially is facing the invalidation of thousands of SEC ALJ adjudications and many additional litigated issues concerning the scope and extent of such invalidations. It will be interesting to see what positions are taken on this issue by a new SEC chair and a new presidential administration.

On July 13, 2016, the SEC adopted amendments to its rules of practice governing administrative proceedings. The amendments address, among other issues, the timing of hearings in administrative proceedings, entitlement to depositions, the admissibility of evidence, and the contents of an answer. In a press release issued the same day, then SEC Chair Mary Jo White stated, “The amendments to the Commission’s rules of practice provide parties with additional opportunities to conduct depositions and add flexibility to the timeliness of our administrative proceedings, while continuing to promote the fair and timely resolution of the proceedings.” The amendments became effective September 27, 2016, and apply to all proceedings initiated on or after that date. The amended rules also apply to pending cases in certain instances depending on their stage.

### Significant Changes

The most significant changes to the SEC rules of practice relate to the timing of hearings and entitlement to depositions. The SEC’s rush to trial in administrative proceedings has been sharply criticized by defendants who contend that the accelerated timeline favors the SEC, which has several years to conduct its own investigation and build its case, and thus disadvantages defendants who have a limited amount of time to prepare their defenses. The recent changes include an amendment to Rule 360, which governs the filing of an initial decision by the hearing officer and the timing of the initial stages of the administrative proceeding.

Under former Rule 360, the initial decision of the hearing officer had to be filed within 120, 210, or 300 days from the date of the service of the order instituting proceedings (OIP). Under the former rule, the more time the parties were afforded for pretrial preparation and motion practice, the less time the hearing officer had to prepare and file the initial decision, which incentivized compressing the pretrial schedule. By contrast, under amended Rule 360(a)(2)(i), the trigger date for the time to file the initial decision is either 30, 75, or 120 days from the date of the completion of post-hearing or dispositive motion briefing or a finding of a default.

Amended Rule 360(a)(2)(ii) also extends the length of the prehearing period from a maximum of four months to 10 months. Notably, the SEC rejected commenters’ entreaties for an open-ended and flexible prehearing period to be determined by hearing officers and stated that the SEC “continue[s] to believe that timely completion of proceedings can be achieved more successfully with express deadlines for completion of the various steps in the administrative proceeding.” Although Amended Rule 360 affords defendants additional time to prepare their cases, even the maximum prehearing period of 10 months is a relatively short period of time to prepare for a complex trial.

With respect to depositions, Amended Rule 233 now permits parties in 120-day proceedings the right to notice three depositions, of up to seven hours each, per side in a single-defendant case and five depositions per side in multidefendant cases. Under Amended Rule 233(a)(3)(ii), the parties are permitted to seek leave to notice up to two additional depositions based on a showing of a “compelling need.” The depositions of witnesses unavailable to testify at the hearing do not count against each party’s limit. Amended Rule 233 presents a marked shift from the former Rule 233 that only permitted parties to take the deposition of an unavailable witness and only with the permission of the ALJ. Defendants in 30-day or 75-day proceedings still have no right to take depositions. By contrast, under Federal Rule of Civil Procedure 30, a party may notice up to 10 depositions without leave of court. Commenters criticized the “one-size fits all” approach of providing a fixed number of depositions and argued that “hearing officer discretion in the matter of depositions is necessary because each case presents unique facts and circumstances.”

The right afforded the parties by Amended Rule 233 to take a limited number of depositions in 120-day proceedings will not dampen criticism concerning the lack of due process in administrative proceedings. The SEC’s recent amendments also clarified the standards for admissibility of evidence. Under former Rule 320, all evidence was admissible in administrative proceedings unless it was “irrelevant, immaterial or unduly repetitious.” Amended Rule 320(a) also excludes evidence that is unreliable. In addition, Amended Rule 320(b) clarifies that hearsay may be admitted if it is “relevant, material, and bears satisfactory indicia of reliability so that its use is fair.” The admission of hearsay evidence in administrative proceedings continues to be more permissive than under the Federal Rules of Evidence. Commenters warned that the proposed rule, which the SEC adopted, would “fail to offer any meaningful protection” and “provide[s] insuffcient guidance and [is] prone to unfair application.”

While some of the SEC’s amendments provide limited protections to defendants, at least one of the amendments imposes a burden on defendants. Amended Rule 220 requires a defendant to disclose in its answer to allegations in an OIP whether the defendant intends to assert a so-called reliance defense, such as reliance on advice of counsel. Failure to make this disclosure in an answer may be deemed to constitute a waiver of the defense. Asserting a reliance on advice of counsel defense requires careful consideration as it involves waiving the attorney-client privilege. Such decisions rarely can be made up front.
in an administrative proceeding but require the benefit of discovery, including depositions and document production, before a defendant can thoughtfully consider if he or she wishes to make this defense. Requiring this defense to be asserted early in the process or risk waiver may be viewed as unfair and as an attempt by the SEC to gain insight into defendants’ trial strategy very early in the matter. For these reasons, Amended Rule 220 is troubling to defendants and their counsel and seems to go backwards in terms of addressing due process concerns.

Legislative Efforts
Legislators have also joined the chorus of critics of the SEC’s use of administrative proceedings. On October 22, 2015, Republican Congressman Scott Garrett of New Jersey introduced a bill titled the Due Process Restoration Act of 2015. This proposed legislation would amend the Securities and Exchange Act of 1934 to permit a defendant within 20 days of notice of an administrative proceeding against him or her to terminate the administrative proceeding if the agency has brought charges seeking a cease-and-desist order and a civil penalty. The bill was formally introduced in the House of Representatives on September 9, 2016. A House committee approved the bill on September 12, 2016, and the bill was then referred to the Subcommittee on Regulatory Reform, Commercial and Antitrust Law and the Subcommittee on Commodity Exchanges, Energy, and Credit. The Financial Choice Act affords defendants in SEC administrative proceedings the right to remove the SEC’s case against them to federal district court. While these legislative efforts are proceeding at a relatively slow pace, it remains to be seen if President Trump will press for a repeal of Dodd-Frank, which could accelerate the legislative process.

Round two’s circuit split may deepen as other circuit courts of appeals consider whether to side with *Lucia* or *Bandimere*. While those cases are underway and the process of seeking review of this issue by the U.S. Supreme Court proceeds, it is clear that the SEC appears to be losing on the ALJ issue in the court of public opinion. Critics wonder why when the consequences of an administrative proceeding are so dire does the SEC not elect to have such matters heard on a level playing field by the independent federal judiciary and juries. Critics also wonder if the SEC has chosen to proceed more frequently in the administrative arena rather than in the courts because it is easier for it to prevail there and to control the development of the securities laws. At least one federal judge has made the point that using administrative proceedings more frequently than the federal courts impedes the growth and development of the securities laws in the federal courts, which is to the detriment of the public.

In the face of these questions, adverse publicity for the SEC, and a new president along with anticipated leadership changes at the highest levels of the SEC, it is unclear whether judicial resolution of these issues or legislative developments will come first. Judicial resolution will decide whether SEC ALJ adjudications performed in the past were done contrary to the U.S. Constitution.
and if so, what will happen to the thousands of past SEC ALJ adjudications. Legislative efforts may permit a defendant in the future to select whether to proceed in an administrative proceeding or in federal court. When faced with such a choice, defendants are bound to choose the federal courts every time.

1 See Jean Eaglesham, SEC Wins In-House Judges, WALL ST. J. (May 6, 2015) [hereinafter Eaglesham]. See also C. Mixter, The SEC’s Administrative Law Enforcement Record, 49 REV. SEC. & COMMODITIES REG. 6 (Mar. 23, 2016) (from 2006-2015, observing the SEC’s increasing election of an administrative proceeding rather than a federal court action; over 87% success rate for SEC in administrative proceedings that rises to 91% when the SEC’s own review process is taken into account). One professor, however, has contended that the high success rate for the SEC in administrative proceedings from 2010-2015 “can be attributed to the routine nature of most of the cases filed administratively.” David Zaring, Enforcement Discretion at the SEC, 94 TEX. L. REV. 1155, 1183 (2016).

2 See Andrew Ceresney, Remarks to the American Bar Association’s Business Law Section Fall Meeting (Nov. 21, 2014), available at https://www.sec.gov. A recent article analyzing the SEC’s contested ALJ proceedings in 2015-16 suggests that the SEC recently has limited its use of its authority under Dodd-Frank to bring actions to an ALJ as opposed to federal court. If this is true, the SEC has pulled back on ALJ proceedings silently. The analysis states “[i]t is unclear whether the agency has restrained its use of its Dodd-Frank [administrative proceeding] authority based on a litigation strategy, as it waits for appellate courts to resolve the pending legal challenges, or a broader reluctance to transfer a large portfolio of its litigation docket to the administrative forum.” However, the data outlined in the article is very small and insufficient to draw any definitive conclusions at this time. See David Kornblau and Sarah MacDougall, SEC In-House Practice Going Back To ‘Old Normal’, Law360 (Nov. 18, 2016), available at https://www.law360.com. See also Eaglesham, supra note 1.


4 U.S. CONST. art. II, §2. For a discussion of the cases raising the Appointments Clause issue see infra at 4-6.


10 Id.

11 Id., slip op. at 11(D.C. Cir. Aug. 9, 2016).

12 Id., Petitioners’ Opening Brief at *35-36 (D.C. Cir. Apr. 13, 2016) (citation omitted).


15 Id. (citation omitted).

16 Id. at 15.

17 Bandimere v. SEC, No. 15-9586 (10th Cir. Dec. 27, 2016).

18 Id., slip op. at 28.

19 Id. at n.36; see also id., concurring op. at 11 (referring to the Commission’s review of ALJ adjudications as “faux de novo review”).

20 Id., slip op. at n.36.

21 Id. at 37.
Reflections on the Plight of an Alternate Juror

I was riveted by the proceedings and felt that I was fulfilling my duty as a citizen. How then was it possible that I would not have an opportunity to deliberate when the case went to the jury? I was nervous and filled with anticipation. Would their decision jibe with my unspoken one? If not, would I understand their reasoning? The answer is mostly “no.” Of the two counts charged against the defendant, the jury voted to acquit on the first and hung on the second, resulting in a mistrial on that count. I would have voted guilty on both counts. After being excused, as we quietly piled into the elevator to get our certificates in the jury assembly room, and made our way to the parking garage, I tried to be philosophical about the process.

One juror then struck up a conversation with my fellow alternate and me regarding our thoughts on the trial, how we as alternates would have voted, and how the juror had voted. After the other alternate left, the juror told me what a terrible experience he had gone through while deliberating, and how he and one or more other jurors had been pressured to change their votes. In addition, he related how the jury foreperson directed the jurors to vote contrary to the court’s jury instructions, which none of the jurors reported to the court. I, however, reported the jury misconduct to the district attorney’s office.

I still wonder what my experience would have been like had I been allowed to deliberate, but it was obviously not meant to be. Just like pinch hitters are necessary in baseball, so are alternate jurors for trials. Still, the experience felt, and feels, a little incomplete. It’s disappointing not to have a voice even if fate stepped in to make it so.

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