UNITED STATES SUPREME COURT

Metro Broadcasting, Inc. v. Federal Communications Commission,

__U.S.__, 90 D.A.R. 7383, No. 89-453 (June 27, 1990).

Supreme Court Narrowly Upholds FCC Minority Preference Policies

In a 5-4 decision, the U.S. Supreme Court upheld two minority preference policies established by the Federal Communications Commission (FCC). First, it is the FCC's policy to award an enhancement for minority ownership and participation in management, which is weighed together with all other relevant factors in comparing mutually exclusive applications for license for new radio or television broadcast stations. Second, the FCC's so-called "distress sale" policy allows a radio or television broadcaster whose qualifications to hold a license have come into question to transfer that license before the FCC resolves the matter in a noncomparative hearing, but only if the transferee is a minority enterprise which meets certain requirements. Metro Broadcasting sought review of an FCC order awarding a new television license to Rainbow Broadcasting in a comparative proceeding, based on the ruling that the substantial enhancement granted Rainbow because of its minority ownership outweighed factors favoring Metro.

The FCC adopted these policies in an attempt to satisfy its obligation under the Communications Act of 1934 to promote diversification of programming, taking the position that its past efforts to encourage minority participation in the broadcast industry had not resulted in sufficient broadcast diversity, and that this situation was detrimental not only to the minority audience but to all of the viewing and listening public.

The Court held that these policies do not violate equal protection principles, since they bear the imprimatur of longstanding congressional support and direction and are substantially related to the achievement of the important governmental objective of broadcast diversity. Writing for the five-member majority, Justice Brennan stated that the strict scrutiny test does not apply, because the FCC's minority ownership programs "have been specifically approved—indeed, mandated—by Congress," and the benign race-conscious measures are constitutionally permissible to the extent that they serve important governmental objectives within the power of Congress and are substantially related to achievement of those objectives.

Justice O'Connor, joined by Justices Rehnquist, Scalia, and Kennedy, dissented on grounds that (1) the Constitution requires that the standard of strict scrutiny be applied to evaluate such racial classifications; and (2) the minority preference policies were not narrowly tailored to address a compelling state interest.

NINTH CIRCUIT COURT COURT OF APPEALS

Geary, et al. v. Renne, et al.,

911 F.2d 280, 90 D.A.R. 9032, No. 88-2875 (August 14, 1990).

Ninth Circuit Strikes Down California's Ban on Party Endorsements for Nonpartisan Offices

In this proceeding, plaintiffs were ten registered voters of the City and County of San Francisco, an organization of registered voters, and one of that organization's officers. The basis of their complaint was the refusal of the City and County of San Francisco and the San Francisco Registrar of Voters to permit official party and party central committee endorsements to be printed in the San Francisco Voter Pamphlet prepared for elections scheduled for June 2 and November 3, 1987. Defendants based their refusal to print such endorsements on the language of Article II, section 6(b) of the California Constitution, which provides that no political party or party central committee may endorse, support or oppose a candidate for nonpartisan office.

In reversing an earlier decision by a panel of the Ninth Circuit (see CRLR Vol. 9, No. 4 (Fall 1989) p. 139 for background information) and affirming the district court, the Ninth Circuit Court of Appeals, en banc, held that Article II, section 6(b) violates the first and fourteenth amendments of the federal Constitution. Writing for the majority, Chief Judge Goodwin concluded that (1) the state's interest in preserving the nonpartisan nature of California's system of electing local and judicial officials is not a compelling state interest; and (2) the ban on party endorsements is not narrowly tailored to achieve these purposes.

Distinguishing *Austin v. Michigan Chamber of Commerce*, __U.S.__, 110 S.Ct. 1391 (1990), which upheld restrictions on independent expenditures by corporations in state candidate elections, the majority stated that those restrictions were aimed at preventing financial fraud and corruption, whereas the ban on party endorsements was directed toward restricting the flow of political information. Relying on its prior decision in *Eu v. San Francisco Democratic Cent. Comm.*, 826 F.2d 814 (9th Cir. 1987), *aff'd*, 489 U.S. 214 (1989), invalidating a similar ban on party endorsements in partisan primaries, the court ascribed no significance to the fact that the offices at issue in *Geary* were nonpartisan. "The concern in *[Eu]* was with the State's abridgment of the rights of political parties and their members to exchange ideas and information, not with the nature of the elections at issue." The majority also noted that there are less drastic means for safeguarding the nonpartisan nature of local and judicial elections, including provisions for nonpartisan methods of nominating candidates for office and controls on partisan activities of candidates.

In a dissenting opinion, Judge Rymer, joined by Judges Alarcon and Fernandez, found that the state has a compelling interest in the structure of its nonpartisan government and that Article II, section 6(b) is essential to preserving that structure. In a separate dissent, Judge Alarcon criticized the majority for failing to consider the evidence in the record and in California history concerning "the devastating impact party endorsements can have on the integrity of local office holders and the independence of the judiciary."

UNITED STATES DISTRICT COURTS

Service Employees Int'l Union v. Fair Political Practices Commission,

__F.Supp.__, 90 D.A.R. 11170, No. CIV. S-89-433-LKK (Sept. 25, 1990).

Federal Court Invalidates Proposition 73's Campaign Contribution Limits

Just six weeks before election day, U.S. District Court Judge Lawrence K. Karlton of the Eastern District of California struck down the contribution limits applicable to all campaigns for election to state and local office established in Proposition 73, passed by the voters in June 1988. (See CRLR Vol. 9, No. 4 (Fall 1989) pp. 140-41 and Vol. 8, No. 2 (Spring 1988) p. 1 for extensive background information on Propositions 68 and 73, two campaign reform initiatives approved by the electorate in June

1988.)

Proposition 73 established limitations on campaign contributions that may be made or accepted during any fiscal year, defined as the period between July 1 and June 30. It also limited candidates to raising funds for a particular office, and set forth procedural requirements regarding establishment of a campaign bank account and reporting to the FPPC. Finally, it prohibited the transfer of funds between candidates and controlled committees of a single candidate.

Three incumbent legislators sponsored Proposition 73. In this action (one of numerous lawsuits seeking to invalidate all or parts of both Propositions 68 and 73), the original plaintiffs—challenging the contribution limits as violative of their first amendment rights of speech and association—were a number of incumbent legislators, various campaign committees, labor organizations, and a contributor to political campaigns. The Democratic Party also intervened as a plaintiff, arguing that the provisions of Proposition 73 which prohibited it from contributing more than $5,000 to any candidate in any fiscal year, or from accepting contributions of more than $2,500 from any one person in any fiscal year for the purpose of making contributions to a particular candidate, hindered it from engaging in voter registration and membership communication activities regarding its endorsement of candidates.

The court engaged in a sequential analysis: it first examined whether the challenged provisions of Proposition 73 impinge upon rights protected by the first amendment; then, it examined whether there is a sufficiently strong governmental interest served by the statute's restriction on those rights; finally, it determined whether the provisions are "narrowly tailored to the evil which may be legitimately regulated."

The court first found that Proposition 73's fiscal year contribution limitations "in and of themselves constitute a burden upon First Amendment activity." The court noted that the only governmental interests deemed important enough to outweigh a first amendment restriction were (1) limiting the actuality or appearance of corruption in elections; and (2) limiting the "corrosive and distorting effects of immense aggregations of wealth that are accumulated with the help of the corporate form and that have little or no correlation to the public's support for the corporation's political ideas," from the recently decided *Austin v. Michigan Chamber of Commerce*, ___U.S.___, 110 S.Ct. 1391 (1990).

Thus, plaintiffs contended that the limitations on contributions measured by fiscal year, rather than by election, worked an unconstitutional preference for incumbents and against challengers. The justification for the fiscal year structure put forth by defendants was that it allows any candidate who is successful in the June primary to receive more contributions in the November general election from persons who gave the maximum allowable contributions for the primary election. In both its 208 findings of fact and its conclusions of law, the court found that this arrangement provides a major benefit to incumbents—the very evil Proposition 73 purports to ameliorate. Thus, it "clearly fails the legitimate governmental interest and narrow tailoring test...." The court then found the fiscal year contribution limitations inseverable from the contribution limit provisions in general, and thus struck down all provisions of Proposition 73 relating to limitations on campaign contributions.

The court's basic holding is based on the fact that incumbents are in a position to solicit and receive $1,000 each fiscal year from their supporters as they hold office—building up an intimidating fund to deter challenge. For a state senator, this continuous gathering of funds allows $5,000 from each individual contributor in any given term of office, since there are five fiscal years within the four-calendar-year term of a senator. In contrast, when a challenger appears during an election year to challenge such an incumbent, he/she is effectively subject to a $1,000 limit per individual contributor. The court found that this system, in fact, operated to deprive challengers of meaningful opportunity to compete. The court implied that the limits of Proposition 68, which are based not on fiscal years but on primary and general elections, respectively, would not create the same constitutional problem, since the limits are applied to both on a more equal practical basis.

The court also invalidated the initiative's ban on transfers of funds between candidates and controlled committees of a single candidate. "It is clear that the ban acts as an expenditure limitation; such limitations have never been upheld, save in connection with the expenditures of corporations."

In the chaos that followed Judge Karlton's September 25 ruling, the FPPC announced that it would immediately begin enforcing the similar campaign contribution limits in Proposition 68 as to legislative races. However, three days after his original ruling, Judge Karlton stayed it as to legislative races, thus reimposing Proposition 73's contribution limits. The original order striking the limits remained effective as to statewide races, thus unleashing a frenzy of fundraising activity and a torrent of campaign contributions to candidates for statewide offices, particularly the hotly-contested gubernatorial race.

Chemical Specialties Manufacturers Association, Inc. v. Allenby,

744 F.Supp. 934, 90 D.A.R. 10903, No. C90-0211-FMS (September 13, 1990).

Proposition 65 Not Preempted by Federal Statutes

Plaintiff, a trade association whose members manufacture a variety of chemical specialty products, filed an action for declaratory judgment, seeking a ruling that the warning requirements of Proposition 65, the Safe Drinking Water and Toxics Enforcement Act of 1986, are preempted by two federal statutes—the Federal Fungicide, Insecticide, and Rodenticide Act (FIFRA), and the Federal Hazardous Substances Act (FHSA). The U.S. District Court for the Northern District of California found that the issue of FIFRA preemption was previously decided in *D-Con v. Allenby*, 728 F.Supp. 605 (N.D. Cal. 1989); in that case, the court found that FIFRA expressly permits state regulation of pesticide sale and use.

With regard to FHSA, the court concluded that "Congress clearly did not intend to occupy this entire area of regulation, as evidenced by the fact that states are expressly allowed certain functions under both FIFRA and FHSA." The court also stated that "[n]o evidence shows the impossibility of complying with both federal and state statutes."

CALIFORNIA COURTS OF APPEAL

Californians for Native Salmon & Steelhead Ass'n v. California Dep't of Forestry, et al.,

221 Cal. App. 3d 1419, 90 D.A.R. 7673, No. A046232 (July 6, 1990).

Action for Declaratory Relief Appropriate in Challenging Alleged "Pattern and Practice" of Unlawful Conduct by Forestry Department

The First District Court of Appeal recently reversed the trial court's dismissal and reinstated an action for declaratory relief challenging the California Department of Forestry's (CDF) alleged policies regarding two issues: (1) the time of filing of CDF's responses to public comments on a timber harvesting plan (THP); and (2) the evaluation and mitigation in each THP of the cumulative impact of logging activities.

In its original complaint, plaintiffs challenged CDF's approval of a specific THP in a combined petition for writ of mandate/complaint for injunctive and declaratory relief. They sought not only to vacate the THP approval, but declaratory relief outside the THP at issue concerning a "pattern and practice" of agency conduct allegedly in violation of the California Environmental Quality Act (CEQA). During the judicial proceeding, the THP grantee withdrew the THP and moved for an order dismissing it as a party. Co-respondents CDF and Board of Forestry demurred to the complaint, arguing that the challenges to the THP were moot and that there was no longer a justiciable controversy "in that the pleading refers to unspecified timber harvest plans and to an unidentified contention or policy of Respondents." The trial court dismissed the THP grantee and sustained the demurrer with leave to amend to make more specific allegations regarding CDF's policies.

Plaintiffs' first amended pleading was a straight complaint for declaratory and injunctive relief, alleging and challenging "the pattern and practice of the California Department of Forestry in their [sic] approval of timber harvest plans, both in their failure to evaluate and respond to comments, and to assess cumulative impacts as mandated by the California courts." Specifically, plaintiffs allege that CDF regularly approves THPs and allows timber operations to commence without issuing written responses to significant environmental objection by the public no more than ten days from the date the plan is approved, contrary to the requirements in sections 1037.7 and 1037.8 of the Forest Practice Rules and CEQA, as interpreted in *EPIC v. Johnson*, 170 Cal. App. 3d 604 (1985), and other cases. Further, plaintiffs allege that, in numerous instances, CDF has failed to address the cumulative impacts of the proposed harvest along with other past, present and proposed harvests, pursuant to CEQA and *EPIC v. Johnson*. Plaintiffs allege a list of 65 approved THPs as illustrative of respondents' "procedure" to issue responses to public comments tardily or not at all, and of respondents' having "consistently ignored" their duty to assess cumulative impacts. Respondents demurred to the amended complaint. The trial court sustained the demurrer, and plaintiffs appealed.

In reversing and remanding for trial, the appellate court held that an action for declaratory relief is a proper vehicle, noting that the material factual allegations of plaintiffs' complaint have been admitted by respondents' demurrer. "Appellants allege and respondents dispute whether CDF is engaged in conduct or has established policies in violation of applicable statutes, regulations, and judicial decisions. Clearly the allegations of appellants' complaint sufficiently set forth an actual controversy over significant aspects of respondents' legally-mandated duties."

In response to CDF's argument that plaintiffs are merely expressing dissatisfaction with a series of 65 THP approvals, the court again noted that plaintiffs allege a "pattern and practice" of conduct violative of the law, which has been admitted by means of respondents' demurrer. The court also rejected respondents' argument that plaintiffs' challenge should be by way of a petition for administrative mandamus; "[a]ppellants...challenge not a specific order or decision, or even a series thereof, but an overarching, quasi-legislative policy set by an administrative agency. Such a policy is subject to review in an action for declaratory relief."

On September 19, the California Supreme Court denied respondents' petition for review. At this writing, this action is proceeding to trial.

Midpeninsula Citizens for Fair Housing v. Westwood Investors, et al.,

221 Cal. App. 3d 1377, 90 D.A.R. 7614, No. H005191 (July 2, 1990).

Sixth Appellate District Upholds Broad Standing to Halt Unlawful Business Practice

Following the lead of the First District Court of Appeal, the Sixth District Court of Appeal held that non-aggrieved persons may sue for injunctive relief under California's unfair competition statute, Business and Professions Code section 17204. In *Midpeninsula*, a nonprofit organization sued under the Unruh Civil Rights Act, Civil Code section 51 *et seq.*, and the unfair competition laws to enjoin an apartment complex rental policy which limited occupancy to one person per bedroom. The court found that Midpeninsula is not a "person aggrieved" within the meaning of the Unruh Act, nor does Midpeninsula have the representative standing to sue under that Act. Citing extensively to *Consumers Union of United States, Inc. v. Fisher Development, Inc.*, 208 Cal. App. 3d 1433 (1989), the court held that—even though the organization lacked standing under the Unruh Act—it could still obtain injunctive relief under the state's unfair competition laws, which provide that "any person acting for the interests of itself, its members or the general public" is entitled to bring an action for injunctive relief from any "unlawful, unfair or fraudulent business practice."

As in the *Consumers Union* case, the court noted that courts have consistently given a broad interpretation to the standing provisions of the unfair competition laws, finding that the narrower standing requirements of the Unruh Act coincide with the treble damages and attorneys' fees available under that Act, while only injunctive relief is available under the broader Business and Professions Code section 17204.

Bily v. Arthur Young & Co.,

222 Cal. App. 3d 289, 90 D.A.R. 8307, No. H003695 (July 20, 1990).

Independent Auditors Liable to Third Party Investors for Professional Negligence

In a case arising from the collapse of the Osborne Computer Corporation, the Sixth District Court of Appeal upheld damages awarded against Arthur Young & Company for its failure to exercise reasonable care as an independent auditor.

In 1981, Osborne engaged Arthur Young & Company to audit its financial statements; plaintiffs subsequently relied on the unqualified audit opinion issued by Arthur Young in January 1983 in making substantial purchases of Osborne stock. Because of significant weaknesses in Osborne's internal accounting procedures, the financial statements were overly optimistic; in 1983, Osborne went into bankruptcy, resulting in substantial losses for the investors. The investors sued Arthur Young for professional negligence.

In upholding the damages awarded to most of the investors, the court rejected Arthur Young's argument that the duty of care owed by independent auditors should be defined solely by generally accepted auditing standards (GAAS) and generally accepted accounting procedures (GAAP). Instead, the court held that GAAS and GAAP served only as "some evidence" of the proper standard of care, and that "it is the general rule that adherence to a relevant custom or practice does not necessarily establish the actor has met the standard of care." The court explained that restricting an auditor's duty strictly to GAAS and GAAP "would inappropriately entrust to the accountancy profession itself the balancing of interests implicit in any determination of duty and breach."

The court also rejected Arthur Young's request to severely narrow the scope of persons to whom auditors owe a duty of care. Citing *International Mortgage Co. v. John P. Butler Accountancy Corporation*, 177 Cal. App. 3d 806 (1986), the court held that independent auditors are liable to "those third parties who reasonably and foreseeably rely on negligently prepared and issued unqualified audited financial statements, regardless of whether the third parties were in contractual privity with, or their reliance was actually foreseen by, the auditor."

The court also held that the trial court correctly denied Arthur Young's motion to exclude all evidence concerning its failure to disclose material weaknesses in Osborne's internal accounting controls, finding that independent auditors are required to assess the sufficiency of an audit client's internal accounting controls and, where material weaknesses exist, to test the accuracy of information provided by the client and inform the senior management, board of directors, and the board's audit committee of the material weaknesses. The court held that evidence of Arthur Young's nondisclosure was relevant to whether the auditor "failed to exercise professional skill sufficient to discover, or had discovered but for whatever reason had mischaracterized or disregarded, the fact that Osborne Computer Corporation lacked adequate internal accounting controls, and in any event had failed to apply auditing tests and procedures sufficient to compensate for the lack of internal controls...."

The *International Mortgage* and *Bily* cases are likely to be important precedents in litigation arising from the collapse of California savings and loans. One important aspect of many insolvent S&Ls is the failure of independent auditors to either detect or take appropriate actions to correct weak internal accounting controls by corrupt or poorly managed thrifts.

Bjornestad v. Hulse, et al.,

223 Cal. App. 3d 507, 90 D.A.R. 10895, No. C007526 (September 5, 1990).

Water District's One-Parcel, One-Vote Election Scheme Violates Equal Protection

In this proceeding, the Sixth District Court of Appeal held Water Code section 30700.6 to be unconstitutional under the equal protection clauses of the California and federal constitutions. Section 30700.6 provides that only one designated landowner per parcel in the Sierra Lakes County Water District —regardless of his/her residency—may vote in a district election or be a member of the district's governing board of directors.

The court found that the county water district had broad public function and governmental powers which distinguished it from the districts in caselaw where property-based restrictions have been upheld, and concluded that the interests of nonlandowning residents were such that they could not be deprived of their right to vote.

County of Sacramento, et al. v. Fair Political Practices Commission,

222 Cal. App. 3d 687, 90 D.A.R. 8525, No. C005845 (July 27, 1990).

Local Campaign Financing Ordinance Preempted by Proposition 73

In this proceeding, the Third District Court of Appeal held that Proposition 73's ban on the use of public funds for political campaigns (codified in Government Code section 85300) prevails over a Sacramento County ordinance providing for limited public financing of supervisorial campaigns. Proposition 73, enacted by the state electorate at the June 1988 general election, amended the Political Reform Act of 1974, and provides in part that no public officer shall expend and no candidate shall accept any public moneys for the purpose of seeking elective office. Section 15-B of the Sacramento Charter provides for partial public financing of contests for county elective offices for those candidates who agree to certain limits on campaign expenditures.

Writing for a unanimous court, Justice Puglia found that (1) "the integrity of election contests is a longstanding matter of statewide interest;" (2) "[b]y its terms Proposition 73 applies to local and statewide elections alike" and was "intended to establish a single statewide body of law pertaining to the financing of election campaigns;" and (3) the ballot materials accompanying Proposition 73 specifically discuss the issue of public campaign financing by local governments. On this basis, the court concluded that "the express language of section 85300 as well as its legislative history manifest a statewide concern with campaign financing which perforce prevails over conflicting local provisions."