



## DEPARTMENT OF CORPORATIONS

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The Department of Corporations (DOC) is a part of the cabinet-level Business, Transportation and Housing Agency and is empowered under section 25600 of the California Code of Corporations. The Commissioner of Corporations, appointed by the Governor, oversees and administers the duties and responsibilities of the Department. The rules promulgated by the Department are set forth in Division 3, Title 10 of the California Code of Regulations (CCR).

The Department administers several major statutes. The most important is the Corporate Securities Act of 1968, which requires the "qualification" of all securities sold in California. "Securities" are defined quite broadly, and may include business opportunities in addition to the traditional stocks and bonds. Many securities may be "qualified" through compliance with the Federal Securities Acts of 1933, 1934, and 1940. If the securities are not under federal qualification, the commissioner must issue a "permit" for their sale in California.

The commissioner may issue a "stop order" regarding sales or revoke or suspend permits if in the "public interest" or if the plan of business underlying the securities is not "fair, just or equitable."

The commissioner may refuse to grant a permit unless the securities are properly and publicly offered under the federal securities statutes. A suspension or stop order gives rise to Administrative Procedure Act notice and hearing rights. The commissioner may require that records be kept by all securities issuers, may inspect those records, and may require that a prospectus or proxy statement be given to each potential buyer unless the seller is proceeding under federal law.

The commissioner also licenses agents, broker-dealers, and investment advisors. Those brokers and advisors without a place of business in the state and operating under federal law are exempt. Deception, fraud, or violation of any regulation of the commissioner is cause for license suspension of up to one year or revocation.

The commissioner also has the authority to suspend trading in any securities by summary proceeding and to require securities distributors or underwriters to file all advertising for sale of securities with the Department before publication. The commissioner has particularly broad civil in-

vestigative discovery powers; he/she can compel the deposition of witnesses and require production of documents. Witnesses so compelled may be granted automatic immunity from criminal prosecution.

The commissioner can also issue "dissent and refrain" orders to halt unlicensed activity or the improper sale of securities. A willful violation of the securities law is a felony, as is securities fraud. These criminal violations are referred by the Department to local district attorneys for prosecution.

The commissioner also enforces a group of more specific statutes involving similar kinds of powers: the Personal Property Brokers Law (Financial Code section 22000 *et seq.*), Franchise Investment Law (Corporations Code section 31000 *et seq.*), Security Owners Protection Law (Corporations Code section 27000 *et seq.*), California Commodity Law of 1990 (Corporations Code section 29500 *et seq.*), California Credit Union Law (Financial Code section 14000 *et seq.*), Industrial Loan Law (Financial Code section 18000 *et seq.*), Escrow Law (Financial Code section 17000 *et seq.*), Check Sellers, Bill Payers and Proraters Law (Financial Code section 12000 *et seq.*), Securities Depository Law (Financial Code section 30000 *et seq.*), Consumer Finance Lenders Law (Financial Code section 24000 *et seq.*), Commercial Finance Lenders Law (Financial Code section 26000 *et seq.*), Knox-Keene Health Care Service Plan Act of 1975 (Health and Safety Code section 1340 *et seq.*), and the Workers' Compensation Health Care Provider Organization Act of 1993 (Labor Code section 5150 *et seq.*).

### MAJOR PROJECTS

**DOC Continues to Deliberate Sufficiency of Blue Cross' Proposed Public Benefit Plan.** At this writing, DOC Commissioner Gary Mendoza continues to deliberate the legal sufficiency of the public benefit plan belatedly proposed by Blue Cross of California (BCC) after its conversion from nonprofit to for-profit status. Under California law, nonprofit organizations are required to include in their articles of incorporation a promise that, if and when they choose to convert to for-profit status, they will transfer an amount equal to the total value of their assets to the sort of charitable purposes for which they were formed. Under the Knox-Keene Health Care Service Plan Act of 1975, DOC is responsible for adopting procedures which nonprofit entities must follow when they convert to for-profit entities, and for reviewing and approving conversion proposals. In 1991, BCC presented DOC with a plan to "restructure," rather than convert, from

nonprofit to for-profit status, by placing 90% of its assets into a for-profit entity. Under this plan, BCC would remain in existence as a nonprofit entity, but its for-profit subsidiary called WellPoint Health Networks would conduct its HMO business. After more than a year of negotiations and some modifications to the proposed plan, then-DOC Commissioner Tom Sayles approved Blue Cross' new status without requiring BCC to transfer an amount equal to its full value—estimated at \$2.5 billion—to charitable purposes.

During 1994, however, Commissioner Mendoza, a group of public interest organizations, and Assemblymember Phil Isenberg—all dissatisfied with BCC's maneuvering—have taken action to force Blue Cross to return its assets to charity as required by law. Following months of pressure, Blue Cross finally submitted a public benefit plan to DOC in September 1994, in which it promised to turn over \$2.1 billion in assets to a charitable foundation called the California HealthCare Foundation, which in turn would make grants to qualified health care programs and projects. DOC solicited public comments concerning Blue Cross' proposed public benefit plan, and received 180 comments by October 31, 1995. Most comments express concern that no independent assessment of the value of Blue Cross' nonprofit assets has ever been conducted; that the plan must prohibit employees, officers, and directors of Blue Cross and WellPoint from serving on the Foundation's board; and that the Foundation should be incorporated as a 501(c)(3) nonprofit organization rather than as a 501(c)(4) organization (as desired by Blue Cross), because the latter type of nonprofit is permitted to lobby and engage in other forms of advocacy. [15:1 CRLR 106-07; 14:4 CRLR 116-17]

At this writing, Commissioner Mendoza is still reviewing Blue Cross' proposed plan. Among other things, Mendoza has stated that he is considering the implications of the incorporation of the Foundation as a 501(c)(4) organization as opposed to a 501(c)(3) organization.

In a related action, WellPoint and Health Systems International, Inc. (HSI), a 1.6-million-member HMO, announced in early April that they had entered into a merger agreement; the merger would create the country's largest publicly-traded managed care provider. The combined company, which would operate under the Blue Cross logo, would have 4.4 million members and approximately \$6 billion in annual revenue; under the proposed deal, the combined company would transfer \$3 billion in cash and stock to two new nonprofit



foundations, the goal of which would be to expand health care for low-income Californians. At this writing, the proposed merger must be approved by state and federal regulators, including DOC, before it may take effect; the regulators' decision on the merger is not expected until fall.

**Offer and Sale of Securities by Small Businesses.** On January 27, Commissioner Mendoza published notice of his intent to amend DOC's regulations under the Corporate Securities Law (CSL) of 1968 relating to small businesses. Corporations Code section 25113(b)(2) provides for a modified permit application process for small companies intending to raise up to \$1 million in any 12-month period through the offer and sale of securities to the public; the provision was intended to facilitate the raising of capital and job creation by small businesses in California and increase access of small business issuers to the capital markets. Section 25113(b)(2) was also intended to complement the Small Corporate Offering Registration (SCOR) procedures approved by the North American Securities Administrators Association (NASAA) and adopted by various other states. Since the enactment of section 25113(b)(2), however, fewer than twenty application filings have been made under that section.

Based upon discussions with filers and potential filers, Commissioner Mendoza found that the standards applied by DOC fail to recognize the often extensive personal contribution made by the promoters to the success of the enterprise, the market realities of finding a selling agent for the securities of small companies, and the often limited need for audited financial statements when the issuer is a small enterprise. The Commissioner has proposed the following amendments in order to facilitate capital formation and job creation by small businesses in California, and to bring about greater uniformity in regulatory standards among the states:

- Section 260.001, Title 10 of the CCR, would be amended to add subsection (i) to define the term "small business issuer." As defined by proposed subsection (i), a "small business issuer" must be a California corporation or a foreign corporation subject to Corporations Code section 2115 that meets the "small business concern" criteria found in 15 U.S.C. section 632(a) and 13 C.F.R. Part 121, is not an investment company or "blind pool" company, and, if a majority-owned subsidiary, the parent must also be a small business issuer. Also, subsection 260.001(a) would be amended to include articles of organization of limited liability companies, which are now recognized as business entities under California law.

- Section 260.140.01(e), Title 10 of the CCR, would be adopted to provide investor suitability standards for a small business issuer. Under proposed subsection (e), when the proposed maximum aggregate offering does not exceed \$5 million, the requirements under section 260.140.05 (except for proposed subsection (c)), 260.140.31, and 260.140.50 (except for the requirement that the initial offering price shall not be less than \$2 per share) are waived if the securities are sold to (1) investors having either a minimum net worth of \$150,000, or a minimum net worth of at least \$75,000 and a minimum gross income of \$50,000 (either during the last tax year or, based upon a good faith estimate, during the current tax year); and (2) to a small investor who has not purchased more than \$2,500 of securities in the twelve months before the proposed sale; or (3) to both (1) and (2).

- Currently, section 260.140.05, Title 10 of the CCR, provides that an application for an open qualification will be denied if the business in which the issuer is engaged is not anticipated to produce profits within a reasonable period of time or if the business operation depends upon the development of a product or system which will not be completed before the offering begins. Section 260.140.05 would be amended to provide that 24 months after the application becomes effective is a "reasonable period of time" for determining whether a business will produce profits; a longer period of time may be authorized under certain circumstances. According to DOC, this will allow the issuer to file for an extension of time. DOC also proposes to repeal existing language which provides that an open qualification will be denied if the development of a product or system upon which the business depends has not been completed prior to the commencement of the offerings.

- Proposed new section 260.140.05(b) would require that prospective financial information be prepared by the issuer and based upon appropriate and reasonable assumptions. The Commissioner may require that the prospective financial information be reviewed by an independent certified public accountant.

- Proposed new section 260.140.05(c) would require that small business issuers deliver a copy of the pamphlet, *A Consumer's Guide to Small Business Investments*, to each prospective purchaser at least five business days before a prospective investor's offer to purchase securities is accepted. This guide is published by NASAA and is available from that organization or from any of DOC's offices.

- Currently, section 260.140.20, Title 10 of the CCR, sets forth reasonable sell-

ing expenses. The Commissioner proposes to amend the reasonable selling expenses for small business issuers. New section 260.140.20(b) would allow reasonable selling expenses of 18% of the aggregate offering price when the maximum aggregate offering price does not exceed \$5 million anywhere, providing that the total underwriting and brokerage discounts and commissions do not exceed 13%. Proposed section 260.140.20(c) would allow reasonable selling expenses of 20% of the aggregate offering price when the maximum aggregate offering price for all securities does not exceed \$3 million anywhere, providing that the total underwriting and brokerage discounts do not exceed 15%.

- Section 260.140.31, Title 10 of the CCR, provides that a number of promotional shares which do not exceed 25% of all of the common shares issued and proposed to be issued by the corporation which is a small business issuer is presumptively reasonable. DOC's proposed amendments would raise the limit of promotional shares to 50%, if an issuer meets the conditions for filing under Corporations Code section 25113(b)(2).

- Section 260.613, Title 10 of the CCR, requires audited financial statements for all open qualifications. Proposed amendments to subsection 260.613(b) would delete the reference to "independent public accountant," as this term is outdated and rarely used. In addition, the Commissioner proposes to adopt new subsection 260.613(f) to allow a small business issuer to use "reviewed financial statements" if the aggregate proceeds of the proposed offering plus the total aggregate proceeds to the issuer from the sale of any of its securities in the preceding twelve months is not more than \$500,000; the term "reviewed financial statements" means financial statements prepared and accompanied by a report issued by an independent certified public accountant prepared in accordance with generally accepted accounting principles. However, the Commissioner will retain the authority to require audited financial statements.

At this writing, the public comment period on these proposed amendments ended on March 17, and the amendments now await approval by the Commissioner and the Office of Administrative Law (OAL).

**Sale of Securities to "Qualified Purchasers."** On February 3, the Commissioner published notice of his intent to adopt new sections 260.102.16, 260.102.17, 260.102.18, and to amend sections 260.103(b), 260.113.1(b), 260.102.10.1, and 260.102.15, Title 10 of the CCR, to implement SB 1951 (Killea) (Chapter



828, Statutes of 1994). That bill enacted Corporations Code section 25102(n), which provides that an offer and sale of a security in a limited public offering to certain "qualified purchasers" may be exempted from the Commissioner's review and approval process provided specified requirements are met. This exemption is unique in that it allows for the publication of a notice announcing the proposed offer of securities; only those investors who meet the specified qualifications may purchase these securities. [15:1 CRLR 108; 14:4 CRLR 119]

In addition to the general announcement, the issuer must file a notice of transaction with the Commissioner concurrently with the publication of the general announcement of the proposed offering or at the time of the initial offer of securities, whichever occurs first; the notice must be accompanied by a \$600 filing fee. This exemption is not available for transactions in which the issuer failed to file the first notice or fails to pay the filing fee. A second notice must be filed within ten business days following the close or abandonment of the offering, but in any case no more than 210 days from the date of the filing of the initial notice.

New section 260.102.16, Title 10 of the CCR, would set forth general information on these notices, the form of the notices, and the instructions for completing the notices. Among other things, the section would set forth general filing requirements for the first and second notices; define the term "blind pool issuer"; contain the form of the first notice required by Corporations Code section 25102(n)(7)(A) and include instructions for filing the first notice with the Commissioner; and contain the form of the second notice required by Corporations Code section 25102(n)(7)(B) and include instructions for filing the second notice with the Commissioner.

Corporations Code section 25102(n)(4) requires that a written disclosure statement be received by each natural person in an offering of securities exempt from federal registration under Rule 504 of the Securities Act of 1933. Proposed new section 260.102.17, Title 10 of the CCR, would provide that the written disclosure statement required under section 25102(n)(4) be the Small Corporate Offering Registration Form (Form U-7).

Proposed new section 260.102.18, Title 10 of the CCR, would provide that a purchase for the purchaser's own account, as specified, may include an offer to resell or resale made in compliance with Rule 144A adopted by the Securities and Exchange Commission (17 C.F.R. Part 230.144A).

Proposed amendments to section 260.103(b), Title 10 of the CCR, would include references to Corporations Code section 25102(n) and the notices contained in section 260.102.16.

Currently, section 260.113.1(b), Title 10 of the CCR, contains additional instructions for use of the Small Corporate Offering Registration Form (Form U-7). DOC's proposed amendments to section 260.113.1 would delete the definition of the term "development stage company."

Finally, DOC proposes to make non-substantive and corrective amendments to sections 260.102.10.1 and 260.102.15, Title 10 of the CCR. At this writing, the public comment period on the amendments and additions closed on March 24, and the proposed changes now await adoption by the Commissioner and review and approval by OAL.

**Other DOC Rulemaking Under the Corporate Securities Act.** The following is a status update on other rulemaking proceedings initiated by DOC under the Corporate Securities Act in recent months:

- On April 28, the Commissioner published notice of his intent to adopt new section 260.204.8, Title 10 of the CCR, which would allow commodity trading advisers registered under the federal Commodity Exchange Act, as amended, to advise or exercise trading discretion, or both advise and trade, with respect to foreign currency options listed and traded exclusively on the Philadelphia Stock Exchange without first registering as an investment adviser under Corporations Code section 25230. At this writing, DOC will accept public comments on the proposed action until June 16.

- In December 1994, the Commissioner published notice of his intent to amend sections 260.102.14 and 260.165, Title 10 of the CCR, relating to the limited offering exemption notice under Corporations Code section 25102(f). [15:1 CRLR 107] DOC received public comments on the proposed amendments until February 3; however, the Commissioner has since decided to withdraw this rulemaking proposal.

**Emergency Rulemaking Under the Knox-Keene Health Care Service Plan Act of 1975.** On May 9, OAL approved DOC's emergency adoption of section 1300.71.4, Title 10 of the CCR, which implements SB 1832 (Bergeson) (Chapter 614, Statutes of 1994). Among other things, SB 1832 added section 1371.4 to the Health and Safety Code; section 1371.4(g) requires DOC to adopt emergency regulations regarding the responsibilities of a health care service plan (HCSP) to an enrollee who requires medical care after stabilization

of an emergency medical condition. [14:4 CRLR 119-20]

In order to comply with section 1371.4(g), the Commissioner adopted section 1300.71.4 on an emergency basis. Specifically, section 1300.71.4 will prevent the interruption of, or gap in, health care services, and clarify the responsibilities of health care providers and HCSPs in circumstances where an enrollee continues to require medically necessary health care services after stabilization of the enrollee's emergency medical condition. The section governs circumstances prior to stabilization or during periods of destablization of an enrollee's emergency medical condition when an enrollee requires immediate medically necessary health care services. In this situation, a HCSP is required to pay for such care regardless of whether the emergency health care provider is contracting with the HCSP.

The section also sets forth the responsibilities of a HCSP when an enrollee has stabilized and does not continue to require immediate medically necessary health care services. In this situation, a HCSP shall respond to a noncontracting emergency health care provider's request for treatment authorization within one hour and pay for any medically necessary health care services provided to an enrollee to maintain the enrollee's stabilized condition up to the time that the HCSP actually initiates the enrollee's transfer.

The section also governs circumstances where a HCSP elects to transfer a stabilized enrollee to a participating health care provider. In this case, a HCSP is required to pay for all medically necessary health care services provided to an enrollee to maintain the enrollee's stabilized condition up to the time that the enrollee's transfer is actually initiated.

Finally, the section would clarify that all requests for treatment authorization, all responses to such requests for treatment authorization, and the actual provision of medically necessary health care services shall be fully documented.

The emergency regulation will remain in effect until September 6; at this writing, DOC is expected to publish notice of its intent to permanently adopt section 1300.71.4 in late May.

**Petition Decision Under the Knox-Keene Health Care Service Plan Act of 1975.** On March 15, the Commissioner denied a February 17 petition for rulemaking filed by Manuel Glenn Abascal; the petition asked DOC to adopt rules under the Knox-Keene Act pursuant to Government Code section 11340.6. The petition requested the Commissioner to either adopt a regulation to prohibit "third party



liability" terms found in subscriber and enrollee health care contracts or, specifically, establish rules that are "fair, reasonable, and consistent with the objectives of the Knox-Keene Act" with respect to third party liability terms found in subscriber and enrollee health care service plan contracts. The petitioner contended that if third party liability terms in HCSP contracts are to be allowed under Knox-Keene, then the Commissioner should adopt regulations establishing third party liability provisions, and requiring clear and prominent specified disclosure in advertising or evidence of coverage material used by HCSPs.

In denying the petition, the Commissioner opined that the necessity for the requested regulations had not been established. Further, the Commissioner stated that even if the necessity could be established, it is DOC's "strong view that such standards should be established by the legislature through the enactment of a statute setting forth such standards with specificity."

## LEGISLATION

**H.R. 1058 (Bliley) and S.240 (Domenici)** are federal bills which would enact the Securities Litigation Reform Act of 1995, which seeks to reduce or eliminate the incidence of lawyer-driven litigation against securities dealers or companies. Supporters of the measure generally contend that the Act would make it more difficult for attorneys to bring frivolous suits on behalf of disgruntled shareholders against securities dealers or companies; however, several consumer groups, including the American Association of Retired Persons and the Consumer Federation of America, contend that the measures would also limit meritorious suits and enable companies to be overly-optimistic in their projections and other forward-looking statements by providing more freedom to companies to speculate in promotional literature about future performance. H.R. 1058 was passed from the House of Representatives in March; S.240 is expected to be passed from the Senate in June.

**SB 445 (Rosenthal)**, as amended April 17, would compel the DOC Commissioner to require every nonprofit HCSP to annually submit for review a report summarizing charitable and other public benefit activities undertaken by the plan; require any nonprofit HCSP that intends to restructure in a manner that involves substantial for-profit activities to submit a public benefit program that identifies activities to be undertaken by the plan to meet its nonprofit public benefit obligations, for approval by DOC; require a plan

that intends to convert its activities from nonprofit to for-profit to secure approval from the Commissioner in accordance with certain procedures involving establishing a charitable trust; authorize the DOC Commissioner to charge plans a fee, to be deposited in the State Corporations Fund, to pay the costs of the required review and approval by the Commissioner; require the Commissioner to adopt guidelines to implement its provisions; require DOC to provide the public with notice of, reasonable access to, and an opportunity to comment on public records relating to the restructure and conversion of HCSPs; and provide that specified requirements described above would not apply to a nonprofit HCSP restructure or conversion submitted to DOC for review and approval prior to April 1, 1995. [*S. Floor*]

**SB 454 (Russell)**. Existing law requires every HCSP to establish and maintain a grievance system approved by DOC under which enrollees may submit grievances to the plan. As amended April 18, this bill would instead require every HCSP to establish and maintain grievance systems and would require the expansion of the grievance system to also allow the submission of grievances to the plan by health care providers. This bill would also allow subscribers and enrollees, or their family members or agents, to submit a grievance to DOC for review after compliance with certain procedures, and would require the plan to provide notice of this right to subscribers or enrollees in a prescribed manner. This bill would authorize a health care provider to join with, or otherwise assist, a subscriber or enrollee in submitting the grievance or complaint to DOC and to assist with the Department's grievance process. The bill would require DOC to review the documents submitted, authorize DOC to request additional information and to hold meetings with the parties, and require DOC to send a written report of its conclusions and proposed actions to the subscriber or enrollee, or their family member or agent, and the plan within 60 calendar days. The bill would also authorize the subscriber or enrollee, or their family member or agent, to request voluntary mediation with the plan prior to exercising their right to submit a complaint or grievance to DOC, and would provide that choosing to use mediation services would not affect that right. [*S. Appr*]

**AB 73 (Friedman)**, as amended May 1, would prohibit HCSPs and disability insurers from awarding bonus compensation to any retained person on the basis of that person's denying authorization or payment for services.

This bill would also require the DOC Commissioner to establish and maintain a toll-free telephone number for the purpose of receiving complaints and inquiries regarding HCSPs, and would require every HCSP to publish this toll-free number on every evidence of coverage booklet, or an addendum, together with a statement explaining that the toll-free number is available for the purpose of receiving complaints and inquiries about plans. The bill would require that the plan publish a statement informing subscribers of the procedure together with the toll-free number. [*A. Appr*]

**SB 689 (Rosenthal)**. Existing law requires each HCSP to reimburse the DOC Commissioner for the actual cost of processing the licensure application as well as for other costs incurred by the Commissioner in administering the laws governing the plans including routine financial examinations, medical surveys, and overhead. As amended April 26, this bill would revise this provision to also require each plan to reimburse the Commissioner for costs resulting from administering the grievance and complaint review process, maintaining a toll-free number for consumer inquiries, investigating complaints and conducting enforcement actions, and issuing medical survey reports.

Existing law requires every HCSP to establish and maintain a grievance system approved by DOC under which enrollees may submit grievances to the plan. This bill would require that the grievance system include a requirement for plans to provide enrollees or subscribers with a written statement of the disposition or pending status of the grievance within thirty days of receipt of the complaint, and an expedited review process.

This bill would require DOC to receive, investigate, respond, and take enforcement action regarding complaints, and to encourage voluntary mediation to promote the settlement of unresolved complaints. This bill would require DOC to establish and maintain a toll-free telephone number for receiving inquiries and responding to requests about HCSPs and departmental procedures to resolve grievances and complaints. This bill would also require plans to publish the toll-free telephone number of DOC with certain information on every plan contract, on enrollee and subscriber evidence of coverage forms, and on copies of plan grievance procedures. This bill would require the DOC Commissioner to ascertain patterns of complaints and to evaluate what action should be taken by the Department. This bill would authorize the Commissioner to impose administrative penalties not to ex-



ceed \$200,000 for certain failure to respond to complaints by a plan.

Existing law requires DOC to conduct a periodic onsite medical survey of the health system of each plan at least once every five years. Under existing law, reports of surveys and resulting deficiencies and correction plans are required to be open to public inspection, subject to certain opportunities of the plan to review the survey and correct any deficiencies within certain time periods. This bill would require that the onsite survey be conducted at least once every three years, and include a review of certain information. This bill would also require survey results to be reported by the Commissioner at least once every three years. This bill would require that a summary of the final report's findings be provided free of charge to members of the public. It would also require the Department to conduct a follow-up review within eighteen months after issuance of the final report. The bill would require the public policy procedures of the plan to include a survey of subscribers and enrollees, subject to the prior review and approval by the Commissioner, at least once every two years to identify their views on patient care. [S. *Appr*]

**SB 957 (Watson).** Existing law exempts from licensure certain HCSPs operated by any city, county, city and county, public entity, or political subdivision, or by a joint labor management trust governed by a board of trustees; these exemptions remain in effect only until January 1, 1996. Existing law prohibits these exempt entities from reducing or changing current benefits except in accordance with collective bargaining agreements and from engaging in certain actions relating to administrative costs and contracting. As amended May 10, this bill would, instead, grant an exemption from the Knox-Keene Act to any HCSP or self-insured employee welfare benefit plan operated by a city, county, city and county, local public entity, local political subdivision, or joint labor management trust, as defined, that provides services only to employees of those governmental entities and their dependents, and retirees and their dependents, but not the general public, provides funding for the program, files the appropriate annual financial transaction reports with the Controller pursuant to specified provisions of law, and meets certain additional requirements including (among others) fiscal and consumer protection requirements. The bill would also delete the repeal date for this exemption, repeal the prohibition on reducing or changing benefits, and delete the requirement for the study and the report. The bill would re-

quire DOC or the Controller to notify the plan or trust if it determines that the plan or trust may be in violation of any of the conditions of the exemption, and would provide a procedure for the correction of violations.

Existing law presumes that any person or entity that provides health coverage, whether the coverage is by direct payment, reimbursement, or otherwise, is subject to the jurisdiction of the Department of Insurance unless the person or entity shows that, while providing the services, the person or entity is subject to the jurisdiction of another state or federal entity. This bill would, with certain exceptions relating to unfair or deceptive acts, exempt from the Insurance Code any HCSP or self-insured employee welfare benefit plan operated by any city, county, city and county, local public entity, political subdivision, or joint labor management trust, that is exempt from the Knox-Keene Act pursuant to the above-described provisions. [A. *Health*]

**SB 1151 (Rosenthal).** Existing law defines certain terms relating to HCSPs, including the term "basic health care services." As amended May 15, this bill would include urgent care, including out-of-area coverage, as defined, within the definition of basic health care services. This bill would also require that enrollees be permitted to select as a primary care physician any available primary care physician who contracts with the plan in the service area, as defined, where the enrollee lives or works. [S. *Floor*]

**AB 396 (Speier).** Existing law requires that disability insurance policies and nonprofit hospital service plan contracts that cover hospital, medical, or surgical expenses must include obstetrician-gynecologists as primary care providers if they meet the insurers' written eligibility criteria for all specialists seeking primary care physician status. This requirement applies to policies or service plan contracts that are issued, amended, delivered, or renewed in this state. As introduced February 14, this bill would instead provide that obstetrician-gynecologists must be included as eligible primary care physicians if they meet the insurers' written eligibility criteria for all specialists seeking primary care physician status. [S. *Ins*]

**AB 505 (Villaraigosa),** as introduced February 16, would require that, prior to closing a health facility, reducing or eliminating the level of health services provided, or leasing, selling, or transferring the management of a health facility, the facility or the HCSP providing direct patient care shall provide certain notice regarding those proposed changes to the public and the applicable administering

department, in accordance with certain procedures. This bill would further require that eighteen months after implementation of any of those changes, the facility or HCSP report to the administering department on the impacts of the changes. [A. *Health*]

**AB 490 (Villaraigosa).** Existing law requires HCSPs to provide certain notice to enrollees of the termination of a contract with a medical group or individual practice association. As introduced February 16, this bill would permit an enrollee to disenroll from a plan at any time if the plan discontinues covering services provided by the enrollee's preferred provider or if that provider discontinues providing services through the plan. [A. *Health*]

**AB 1266 (Goldsmith).** Existing law requires the DOC Commissioner to require the use by HCSPs of certain disclosure forms containing specified information. As amended April 17, this bill would add additional information required to be disclosed by plans. [S. *Ins*]

**AB 1841 (Figueroa).** Under existing law, any HCSP, disability insurance policy, or nonprofit hospital service plan that includes terms that require arbitration or provides for waivers or restrictions on the right to a jury trial is required to include a disclosure meeting certain requirements. As amended May 16, this bill would repeal this provision and instead require a HCSP, disability insurance policy, or nonprofit hospital service plan that includes terms that require binding arbitration to settle disputes, or restrict or provide for a waiver of the right to a jury trial to include a disclosure that meets certain requirements including that the disclosure be displayed immediately before the signature line on any enrollment forms created by the plan, or incorporated in the electronic methods of enrollment. It would also require enrollment forms or an electronic enrollment process created by an entity other than the plan to include certain prescribed disclosure information, and would require the group contractholder to, upon request, furnish the plan with the original or a copy of the signed enrollment forms or a hard copy of the electronic or other enrollment form used.

The bill would provide that these disclosure requirements apply to group contracts entered into on or after July 1, 1996, and to subscribers and other enrollees who are enrolled under either a group or individual plan contract on or after July 1, 1996, but would not apply to public employees and annuitants who receive health benefits pursuant to the Public Employees' Medical and Hospital Care Act. [A. *Appr*]

**SB 977 (Solis).** Existing law regulates contracts for medical services which con-



tain provisions for arbitration of disputes regarding the professional negligence of a health care provider, as specified; these provisions expressly provide that they do not apply to HCSP contracts offered by an organization licensed pursuant to the Knox-Keene Health Care Service Plan Act of 1975 which contain specified provisions or offer specified notification procedures. As introduced February 24, this bill would delete that exemption and extend the requirements governing contracts for medical services which contain provisions for arbitration of disputes regarding the professional negligence of a health care provider to HCSP contracts offered by an organization licensed pursuant to the Knox-Keene Health Care Service Plan Act of 1975. [S. *Jud*]

**AB 1203 (Murray).** Existing law prohibits a check casher from charging a fee for cashing a payroll check or government check in excess of 3% if identification, defined as a California driver's license or identification card, is provided by the customer. As amended May 2, this bill would specify that the California driver's license or identification card must be valid. The bill would authorize a check casher to agree to defer the deposit of a check, warrant, draft, money order, or other commercial paper for up to thirty days under specified conditions. [A. *B&F*]

**AB 1023 (Aguilar).** Under the California Credit Union Law, the DOC Commissioner has specified duties, including conducting examinations of credit unions licensed or supervised by the Commissioner. To defray administrative costs, including investigations and supervision, the Commissioner requires every credit union licensed or under the Commissioner's supervision to pay in advance for the ensuing year charges and assessments in accordance with a specified schedule. As amended April 25, this bill would revise that schedule.

Under existing law, if an examination is made or services performed, the credit union examined or for which the services are performed is required to pay to the Commissioner the cost of the examination or service, as specified. This bill would repeal this provision. [A. *B&F*]

**AB 640 (Weggeland).** Existing law sets forth various requirements regarding the giving or receiving of notice, whether oral or written, as applied to notice of special corporate meetings and other forms of notice. As amended May 3, this bill would, among other things, with respect to those notice provisions, specify that, in certain instances, facsimiles, telegrams, electronic mail, and electronic voice mail messages are encompassed within specified terms of

notice. The bill would also revise and recast provisions respecting the reacquisition of shares by a corporation. The bill would revise the shareholders entitled to obtain member information by providing that right to shareholders who hold at least 1% of those voting shares and who are subject to specified rules of the Securities Exchange Act of 1934, by virtue of solicitations of proxies relating to the election of directors of the corporation rather than those who have filed a specified form. The bill would make various other technical amendments. [S. *FI&IT*]

**AB 920 (Cunneen).** Under existing law, a holder of shares or voting trust certificates may bring an action on behalf of a corporation against the board of the corporation if certain requirements are met. One requirement is that the plaintiff allege in his/her complaint the efforts to secure from the board the action that the plaintiff desires. If there has been no effort, the plaintiff must allege the reasons for not making the efforts. As introduced February 22, this bill would instead require that the plaintiff allege a demand to the board and the board's unjustifiable rejection of the demand. If the plaintiff does not make a demand, the plaintiff must allege facts from which the court can conclude that a majority of directors could not be expected to fairly evaluate themselves. The bill would provide that certain allegations, including that a majority of the directors would have to sue themselves, are not sufficient to meet this burden. The bill would also provide that in order to be considered an unjustifiable rejection of a demand, the board must have failed to exercise its business judgment either in considering or in rejecting the demand. [A. *Jud*]

**AB 699 (Cunneen).** Under existing law, the members of the board of directors for a for-profit corporation, nonprofit public benefit corporation, nonprofit mutual benefit corporation, and nonprofit religious corporation may participate in a meeting through use of conference telephone or similar communications equipment, so long as all members participating in the meeting can hear one another, and participation in a meeting under this circumstance constitutes presence in person at that meeting. As amended April 18, this bill would provide that the members of the board of these corporations may also participate in their respective meetings through use of conference telephone, electronic video screen communication, or similar communications equipment if a member participating in the meeting can (1) hear and communicate by voice, or visually communicate with the other members, (2) is provided the means of participating in the discus-

sion of issues before the board, including the capacity to propose, or to interpose an objection, to a specific action to be taken by the corporation, and (3) there is some means of verifying that a person communicating by telephone or video screen is a director entitled to participate in the meeting and that a statement, question, or vote was made by that director and not by another person not permitted to participate as a director. [S. *Ins*]

**AB 919 (Cunneen).** The Corporate Securities Law of 1968 requires certain securities offered or sold in this state to be qualified or exempted, as specified. As amended May 15, this bill would provide that an application for qualification or an amendment to an application may be filed electronically with a typed signature, if within two days of filing, a manually signed signature page is also filed, as specified. A manually signed signature page would not be required if the electronic filing is accompanied by an authorized electronic signature that meets legal requirements. [S. *FI&IT*]

**SB 820 (Russell).** Existing law authorizes licensed escrow agents to establish additional business office locations by, among other things, complying with specified filing requirements with respect to an additional bond or bonds for each additional office location or, in lieu thereof, the filing of a written amendment to extend coverage under an existing bond or bonds, as specified. As amended February 23, this bill would recast the above requirement to instead require, in addition to any additional bonds required by existing law, that the amounts for additional office locations be \$10,000 for the first additional location, and \$5,000 for each additional location; the total maximum aggregate bonding amount would not exceed \$100,000. [A. *B&F*]

**AB 950 (Caldera).** Existing provisions of the Escrow Law exempt from its application brokers licensed by the Real Estate Commissioner while performing acts in the course of or incidental to a real estate transaction in which the broker is an agent or a party to the transaction and in which the broker is performing an act for which a real estate license is required. As introduced February 22, this bill would delete that exemption. [A. *B&F*]

**AB 1646 (Conroy).** The Escrow Law exempts from its provisions, among others, any person licensed to practice law in California who is not actively engaged in conducting an escrow agency, any licensed real estate broker while performing acts in the course of or incidental to a real estate transaction in which the broker is an agent or a party to the transaction and in which the broker is performing an act for which





a real estate license is required, and persons whose principal business is that of preparing abstracts or making title searches, as specified. As amended April 17, this bill would delete the exemption of licensed real estate brokers, and require that every person licensed to practice law in this state, and, to the extent of any exemption under the escrow law, title insurers, underwritten title companies, and controlled escrow companies, that perform escrow activities shall have all escrow trust accounts covered by a fidelity bond in an amount equal to the amount on deposit with the respective entity. [A. B&F]

**AB 1725 (Knight).** Existing law authorizes the DOC Commissioner to charge and collect certain amounts from escrow licensees, as specified. As amended May 1, this bill would provide for those payments to be made in three equal and consecutive monthly installments, as specified. [S. FI&IT]

**AB 775 (Aguiar).** Existing law provides that a licensed escrow agent in referring to corporate licensure under the Escrow Law in any communication, as specified, shall only use a statement, to the effect that the escrow company holds a specified DOC escrow license number. As amended April 24, this bill would instead require the inclusion of that statement when referring to corporate licensure in any communication.

Existing law prohibits Fidelity Corporation and its members from advertising, printing, displaying, publishing, distributing, or broadcasting any statement or representation with regard to a guarantee of trust obligations without first obtaining written approval of the Commissioner of Corporations. This bill would delete that approval requirement and also limit the applicability of the provision to statements and representations in advertisements that are false or misleading or calculated to deceive or misinform the public.

Existing law also provides that any advertising referring to Fidelity Corporation shall state in type not smaller than the largest size of type used in the body of the advertisement a statement to the effect that the Escrow Agents' Fidelity Corporation is a private corporation and is not an agency or other instrumentality of the State of California. This bill would revise that statement. The bill would additionally delete a prohibition against advertising that trust obligations are "protected," "guaranteed," or "insured," and instead specifically authorize members to advertise that they are members of the Escrow Agents' Fidelity Corporation which provides fidelity bond coverage as required under the Escrow Law. [A. Appr]

**AB 661 (Boland).** Existing law sets forth crimes and civil penalties for a violation of the Escrow Law; existing law requires all money deposited into escrow to be maintained as trust funds. As amended April 19, this bill would require the district attorney to prosecute persons who have caused a loss of those trust obligations, as specified. [A. B&F]

**AB 46 (Hauser).** Existing law defines and regulates common interest developments, providing (among other things) that these developments shall be managed by an association, as specified. Existing law regulates the conduct of meetings of the association's boards of directors, including the attendance of association members at these meetings, and the availability to association members of minutes of any board meeting. As amended May 11, this bill would reorganize and expand the scope of the law relating to association board of directors meetings, by creating the "Common Interest Development Open Meeting Act." The bill sets forth the rights and responsibilities of board members as well as association members with respect to meetings, including notice procedures. The bill would also permit the association president or two other members of the governing body to call an emergency meeting. The bill would allow the board to meet in executive session, upon the request of a board member subject to discipline, as specified.

Existing law provides, under specified circumstances, a system for alternative dispute resolution prior to the filing of specified civil actions involving a common interest development. In connection with this dispute resolution, any party to the dispute may initiate the resolution process by serving, in a specified manner, a Request for Resolution. This bill would allow for service of the Request for Resolution by any form of mail providing for a return receipt, in addition to the methods permitted by existing law, and would limit the declarations or findings the mediator is permitted to file, and the court is permitted to consider.

Existing law relating to common interest developments prohibits a governing association from imposing or collecting any assessment, penalty, or fee in connection with the transfer of title or any other interest, except as specified. This bill would permit a managing agent of a common interest development to charge a reasonable fee for documents or services provided in connection with a transfer of title, as specified.

The Mobilehome Residency Law generally regulates the management of mobilehome parks, and the rights of homeowners and tenants in these parks. Under existing

law, a mobilehome may be included within a common interest development. This bill would provide that, with the exception of specified provisions relating to subdivisions, cooperatives, and condominiums, the Mobilehome Residency Law shall not apply to a tenant or resident in a park that is a common interest development, as specified. [S. H&LU]

**SB 186 (Maddy).** The California Residential Mortgage Lending Act regulates the making of residential mortgage loans by specified entities, and requires the licensing of persons who make and service loans on residential real property. As amended April 17, this bill would enable a licensed residential mortgage lender to engage as a principal in the business of buying from or selling to institutional investors, residential mortgage loans, and to engage, pursuant to a written agency contract with certain institutional lenders, in the business of soliciting, processing, or underwriting residential mortgage loans for that lender, by using or advancing the lender's own funds. A licensed residential mortgage lender that contracts with an institutional lender to provide these services would be subject to restrictions on fees and charges made, and to reporting requirements. [S. B&F]

**SB 411 (Calderon),** as amended April 26, would permit a residential mortgage lender licensed under the California Residential Mortgage Lending Act to provide brokerage services to a borrower, if the licensee first enters into a written brokerage agreement. The bill would restrict the licensee from brokering certain types of loans, specify the terms of the brokerage agreement with a borrower, provide remedies to a borrower if a licensee makes a materially false or misleading statement, limit the type of fees or charges that a licensee may impose, and require annual reporting of loans brokered by the licensee under these provisions. Under existing law, a real estate broker who negotiates a loan to be secured directly or collaterally by a lien on real property is required, among other things, to deliver a disclosure statement to the borrower before the borrower becomes obligated to complete the loan, as specified. This bill would provide that these provisions apply to a residential mortgage loan arranged by a residential mortgage lender, as specified. [A. B&F]

## ■ LITIGATION

In *Murray, et al. v. Belka, et al.*, No. 740706 (Orange County Superior Court, filed Dec. 30, 1994), a group of investors in failed First Pension Corporation alleges that, as a lawyer in the mid-1980s, DOC Commissioner Gary Mendoza misled DOC.



[15:1 CRLR 109] The complaint alleges that while he was a lawyer at Latham & Watkins in Newport Beach, Mendoza prepared securities offerings for a First Pension entity and then provided misleading information on the offerings to DOC; the suit also names Latham & Watkins, an employee of a company related to First Pension, and First Pension's three operators, all of whom admitted to fraud in the case in August. The SEC has accused First Pension of losing \$121.5 million of investors' money by misleading them to make investments in mortgages that did not exist. All defendants named in the civil complaint are alleged to have violated California securities laws and to have committed breaches of fiduciary duty and fraud. Specifically, the suit alleges that Mendoza provided legal services to the operators of First Pension from 1992 until shortly before his appointment as DOC Commissioner in July 1993. The suit claims that Mendoza and the other defendants failed to disclose facts concerning the true nature of the limited partnership units sold by the defendants in documents provided to investors on a limited partnership offering sold in the mid-1980s. Commissioner Mendoza called the lawsuit "absurd and contemptible." At this writing, the matter is still pending in superior court.

On March 23, the California Supreme Court dismissed its review of the Second District Court of Appeal's decision in *People v. Charles Keating*, 16 Cal. App. 4th 280 (1993). Keating was found guilty on 17 counts for defrauding investors by encouraging them to buy worthless junk bonds instead of government-insured certificates. [15:1 CRLR 109; 12:4 CRLR 120-21; 12:2&3 CRLR 169] In his appeal to the California Supreme Court (No. S033855), Keating contended that he never personally interacted with investors, and that criminal liability for violations of Corporations Code sections 25401 and 25540 is limited to direct solicitors and sellers. Although the matter was fully briefed, oral argument was never granted. The Supreme Court stated that its decision to hear the appeal was "improvidently granted" and remanded the case to the Second District, where the 1993 decision will stand.

## DEPARTMENT OF REAL ESTATE

*Interim Commissioner:*

*John R. Liberator*  
(916) 739-3684

The Real Estate Commissioner is appointed by the Governor and is the

chief officer of the Department of Real Estate (DRE). DRE was established pursuant to Business and Professions Code section 10000 *et seq.*; its regulations appear in Chapter 6, Title 10 of the California Code of Regulations (CCR). The commissioner's principal duties include determining administrative policy and enforcing the Real Estate Law in a manner which achieves maximum protection for purchasers of real property and those persons dealing with a real estate licensee. The commissioner is assisted by the Real Estate Advisory Commission, which is comprised of six brokers and four public members who serve at the commissioner's pleasure. The Real Estate Advisory Commission must conduct at least four public meetings each year. The commissioner receives additional advice from specialized committees in areas of education and research, mortgage lending, subdivisions and commercial and business brokerage. Various subcommittees also provide advisory input.

DRE primarily regulates two aspects of the real estate industry: licensees (salespersons and brokers) and subdivisions. Pursuant to Business and Professions Code section 10167 *et seq.*, DRE also licenses "prepaid rental listing services" which supply prospective tenants with listings of residential real properties for tenancy under an arrangement where the prospective tenants are required to pay a fee in advance of, or contemporaneously with, the supplying of listings. Certified real estate appraisers are not regulated by DRE, but by the separate Office of Real Estate Appraisers within the Business, Transportation and Housing Agency.

License examinations require a fee of \$30 per salesperson applicant and \$60 per broker applicant. Exam passage rates average 56% for salespersons and 48% for brokers (including retakes). License fees for salespersons and brokers are \$170 and \$215, respectively. Original licensees are fingerprinted and license renewal is required every four years.

In sales, or leases exceeding one year in length, of any new residential subdivisions consisting of five or more lots or units, DRE protects the public by requiring that a prospective purchaser or tenant be given a copy of the "public report." The public report serves two functions aimed at protecting purchasers (or tenants with leases exceeding one year) of subdivision interests: (1) the report discloses material facts relating to title, encumbrances, and related information; and (2) it ensures adherence to applicable standards for creating, operating, financing, and documenting the project. The commissioner will not

issue the public report if the subdivider fails to comply with any provision of the Subdivided Lands Act.

The Department regularly publishes three bulletins. *Real Estate Bulletin*, which is circulated quarterly as an educational service to all current licensees, contains information on legislative and regulatory changes, commentaries, and advice; in addition, it lists names of licensees who have been disciplined for violating regulations or laws. *Mortgage Loan Bulletin* is published twice yearly as an educational service to licensees engaged in mortgage lending activities. Finally, *Subdivision Industry Bulletin* is published annually as an educational service to title companies and persons involved in the building industry.

DRE publishes numerous books, brochures, and videos relating to licensee activities, duties and responsibilities, market information, taxes, financing, and investment information. In July 1992, DRE began offering one-day seminars entitled "How to Operate a Licensed Real Estate Business in Compliance with the Law." This seminar, which costs \$10 per attendee and is offered on various dates in a number of locations throughout the state, covers mortgage loan brokering, trust fund handling, and real estate sales.

The California Association of Realtors (CAR), the trade association joined primarily by agents and brokers working with residential real estate, is the largest such organization in the state. CAR is often the sponsor of legislation affecting DRE. The four public meetings required to be held by the Real Estate Advisory Commission are usually scheduled on the same day and in the same location as CAR meetings.

At this writing, DRE Chief Deputy Commissioner John Liberator continues to serve as Interim Commissioner, following the resignation of former DRE Commissioner Clark Wallace.

## MAJOR PROJECTS

**DRE Revenue Dropping.** Although not dependent on the state budget for its funding, DRE is experiencing financial difficulties due to the severe downturn in California's real estate market, which has resulted in fewer licensees and fewer subdivision buyers; the market downturn has directly affected DRE's revenue, which comes from exam, license, and subdivision fees. DRE currently has 55 vacant employee positions which will remain unfilled due to its decreased revenue. DRE's Enforcement Division has taken the brunt of the impact, according to staff; as the market depressed, the Enforcement Division began to experience increased caseloads,