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MICHAEL DENVER
President
Hollister & Brace
PO Box 630
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T: (805)963-6711
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T: 568-2969
aholderness@co.santa-barbara.ca.us

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25 E. Anapamu Street, #2
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T: (805) 962-5821
jim@jamesgriffithlaw.com

LETICIA ANGUIANO
Associate Counsel
Mechanics Bank
1111 Civic Dr., Ste. 390
Walnut Creek, CA 94596
leticia_anguiano@mechanicsbank.com
T: (925) 256-3067

ERIC BERG
Berg Law Group
3905 State St Ste. 7-104
Santa Barbara, CA 93105
T: (805) 708-0748
eric@berglawgroup.com

JOSEPH BILLINGS
Allen & Kimbell, LLP
317 E. Carrillo Street
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T: (805) 966-1501
dboswell@mullenlaw.com

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gmb@grokenberger.com

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Cappello & Noël LLP
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Santa Barbara, CA 93101
T: (805) 564-2444
lconlan@cappellonoel.com

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Ofc of District Attorney
1112 Santa Barbara St
Santa Barbara, CA 93101
T: (805) 568-2424
bcota@co.santa-barbara.ca.us

STEPHEN DUNKLE
Sanger, Swysen & Dunkle
125 E. De La Guerra, Ste 102
Santa Barbara, CA 93101
T: 962-4887
sdunkle@sangerswysen.com

JENNIFER DUFFY
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222 E Carrillo St #400
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T: (805) 963-0755
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1035 Santa Barbara St Ste 7
Santa Barbara, CA 93101
T: (805) 965-3703
elvia@mcmurraylaw.us

JEFF SODERBORG
Barnes & Barnes
1900 State St Ste M
Santa Barbara, CA 93105
T: (805) 687-6660
jsoderborg@barneslawsb.com

LIDA SIDERIS
Executive Director
15 W. Carrillo Street, Ste 106
Santa Barbara, CA 93101
569-5511; Fax: 569-2888
sblawdirector@gmail.com

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CONTRIBUTING WRITERS
Andrea Anaya
Justice William W. Bedsworth
Nicole Hornick
James A. Lisi
Michael P. McCready
Bruce McIver
Robert Sanger

EDITOR
Eric Berg

ASSISTANT EDITOR
Lida Sideris

MOTIONS EDITOR
Michael Pasternak

VERDICTS & DECISIONS EDITOR
Allegra Geller-Kudrow

PROFILE EDITOR
James P. Griffith

PHOTO EDITOR
Mike Lyons

GRAPHIC DESIGN
Baushke Graphic Arts

PRINT PRODUCTION
Printing Impressions

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Submit all **MOTIONS** matter to Michael Pasternak at pasterna@gmail.com.

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On the Cover

The Santa Barbara County Courthouse, photo by Mike Lyons

Local Immigration Enforcement and Detention

By Andrea Anaya

Increased focus has been placed on local enforcement of federal immigration law. Our own community has seen a rise in the number of individuals detained by Immigration and Customs Enforcement (ICE) for minor offenses.

On February 20, 2017, the Department of Homeland Security (DHS) released the memo "*Implementing the President's Border Security and Immigration Enforcement Improvements Policies*" which sets forth the plan to implement the executive order on "*Border Security and Immigration Enforcement Improvements*".

The DHS memo calls for a massive expansion in detention directing DHS personnel to arrest, apprehend, and initiate enforcement actions against "*any alien whom an immigration officer has probable cause to believe*" has violated the immigration laws.

State and local law enforcement agencies are directed to help federal immigration officers detention efforts through the expansion of the 287(g) program, continued cooperation in the Criminal Alien Program, and the reinstatement of the Secure Communities Program.

Section 287(g) Program

Section 287(g) of the Immigration and Nationality Act authorizes DHS to enter into agreements with local law enforcement agencies to deputize local law enforcement officers with the authority to perform the functions of federal immigration officers.

Local law enforcement agencies have the option of agreeing to one of the following three 287(g) agreements.

The Task Force Model allows deputized officers to question and arrest people they encounter during daily operations who they believe have violated immigration laws.

The Jail Enforcement Model allows deputized officers to interrogate individuals in custody and place immigration detainers on those they believe are in violation of immigration law.

The Hybrid Model utilizes a combination of elements from both the Task Force and Jail Enforcement Models.

Andrea Anaya

Santa Barbara County currently has not entered into a 287(g) agreement. Currently, the Orange County Sheriff's Office is the only local law enforcement agency in California to have a 287(g) agreement with the DHS. As of January 2017, Santa Barbara County Sheriff Bill Brown stated that entering into a 287(g) agreement is "not on the horizon with the Santa Barbara County Sheriff's Office."[1]

Although Santa Barbara does not have a 287(g) agreement, this by no means is the only way that Santa Barbara County law enforcement can collaborate with federal immigration officers to enforce immigration laws.

Criminal Alien Program

The Criminal Alien Program (CAP) is one of ICE's longstanding programs, which predates the newest executive orders on immigration enforcement. CAP allows ICE agents to enter jails and prisons to review booking information, records, and interrogate inmates. ICE can then issue immigration detainers or transfer custody of inmates.

Unlike the Secure Communities Program, discussed below, CAP is not a mandatory program. Participation in CAP is voluntary. It is in the discretion of state and local law enforcement agencies how much, if any, access they choose to give ICE agents to their facilities.

Santa Barbara County Jail grants ICE authorization to enter their facility and make determinations on inmates' immigration status. During an interview with KCOY Channel 12, Sheriff Brown confirmed that, "They [ICE] also come into our jail and they [ICE] also make determinations as to who is and who is not documented."[2] Attorneys with non-citizen clients in custody in Santa Barbara County Jail or returning an ankle monitoring device to Santa Barbara County Jail should be aware that ICE may try to interrogate and detain inmates or review inmate records.

Secure Communities Program

The Secure Communities Program was reinstated by the new administration on January 25, 2017. Under this program, information of every individual taken into custody by local law enforcement is automatically sent to ICE. ICE then uses that information to determine whether

that individual may be removable from the United States. If ICE believes that an individual may be removable they can issue an immigration detainer. Under current directive, ICE is authorized to issue an immigration detainer for any individual in custody in jails or prisons even if the arrest of the individual does not result in a criminal conviction.

The immigration detainer is a request to local law enforcement agencies to notify ICE when the law enforcement agency is set to release the individual from custody (e.g. sentence served, charges dropped). The detainer requests that the law enforcement agency hold that person for up to 48 business hours, after their planned release, so ICE can take custody.

An immigration detainer is not indicative of whether a person is actually removable from the United States. An immigration detainer is a hold ICE places on that individual so that they can look into whether the person can even be removed from the United States. An individual is not in removal proceedings until ICE files a Notice to Appear with the Executive Office for Immigration Review and serves a copy on the respondent.

Protections for Non-Citizens in Custody

48 Hour Custody Limitation

If a state prison or county jail chooses to comply with an immigration detainer request it is only allowed to detain an individual for 48 business hours beyond the time the individual was set to be released from custody[3]. If immigration officers do not take custody within the 48-hour period, the local law enforcement agency must release them. An attorney can contact the detaining authority to request that they release the individual or may file a habeas corpus petition in state court to compel the detaining authority. Failing to release an individual after the 48-hour period may subject the detaining authority to civil lawsuits[4].

SB 2792 Transparent Review of Unjust Transfers and Holds (TRUTH) Act

The TRUTH Act, signed by Governor Jerry Brown in September 2016, is intended to promote due process during interrogations by immigration officials. Under the TRUTH Act, if ICE issues an immigration detainer for an individual in custody they must also provide a copy of the detainer to the individual and/or their attorney. If the law enforcement agency has informed ICE of the intended release date of someone in custody, they must also provide that same notice in writing to the individual and their attorney. Additionally, local law enforcement agencies are instructed that if ICE requests to interview an inmate, the law enforcement agency must provide a written consent to the individual which states, "the purpose of the interview, that the interview is voluntary, and that they may decline to be interviewed or may choose to be interviewed only with his or her attorney present."

AB 4 Transparency and Responsibility Using State Tools (TRUST) Act

The TRUST Act (enacted on January 1, 2014) establishes that law enforcement "shall have discretion to cooperate with federal immigration officials by detaining an individual on the basis of an immigration hold after that individual becomes eligible for release from custody". The TRUTH Act directs state and local law enforcement agencies to limit the use of local resources and only utilize its discretion to enforce a detainer if the individual in custody has ever been convicted of a serious or violent felony, a felony punishable by state prison or other crime listed in the statute (ex: assault, forgery, felony possession of controlled substances, burglary). Prior to enactment of the TRUST Act, law enforcement agencies enforced detainers against individuals arrested for simple possession of a controlled substance, DUI, or minor traffic violations, even if the charges were dropped.

An immigration detainer is merely a request. A state or local law enforcement agency is not required to hold an individual for immigration officers. State and local law enforcement agencies have discretion to choose whether they want to use their resources to hold an individual for immigration officers for 48 hours.

The DHS started to publish the Weekly Declined Detainer Outcome Report. The report lists which law enforcement agencies did not comply with immigration detainer requests. Santa Barbara County was listed on DHS's first published report for failing to comply with one detainer request[5]. The Weekly Declined Detainer Outcome Report fails to list how many detainer requests were issued that week, or for how long the individual was held in custody prior to release. ■

Andrea is an associate attorney with Kingston, Martinez & Hogan LLP. She practices immigration law, specializing in family based immigration and removal proceedings. Andrea received her B.A. in Political Science from the University of California, Santa Barbara and earned her J.D. from the Santa Barbara College of Law. She is a member of the American Immigration Lawyers Association. Andrea can be contacted at andrea@kmhimmigration.com.

ENDNOTES

1 Scott Hennessee, *Santa Barbara County Sheriff speaks on immigration issues,* KCOY, (February 1, 2017), http://www.keyt.com/news/

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Anticouni & Associates is pleased to announce Tristan Verburgt has joined the firm as an Associate Attorney. Mr. Verburgt's practice will focus on employment law litigation where he brings extensive jury trial experience. Mr. Verburgt represents both employers and employees in all phases of litigation, including the firm's discrimination, harassment, retaliation and wrongful termination cases. Partner Nicole Ricotta will continue to oversee our wage and hour class actions.

Anticouni & Associates' practice is limited to workplace law and related litigation with an emphasis on wage and hour class actions. The firm filed the first California wage and hour class action over 30 years ago and has obtained over $175,000,000.00 for California employees in subsequent class action litigations. The firm has been successful in obtaining over $2,750,000.00 in *cy pres* funds for local 501(c)(3) non-profit organization from our wage and hour settlements and judgments.

The firm pays substantial referral fees on wage and hour class actions pursuant to State Bar regulations.

Anticouni & Associates

201 N. Calle Cesar Chavez
Suite 105
Santa Barbara, CA 93103
(805) 845-0864

Arbitration Agreements in Nursing Homes: A Closer Look

By Nicole Hornick

Arbitration, an alternative to public court, has been criticized for decades because of biased decisions generally rendered to favor big business interests. Despite the criticisms, the United States Supreme Court has routinely upheld decisions in favor of arbitration, holding that the Federal Arbitration Act preempts state law. Because of this precedent, states have struggled to find a balance between enforcing arbitration agreements and protecting the rights of their citizens. And, main concerns circling the rights of citizens are the rights owed to elders in long term care nursing homes.

Arbitration Agreements are commonly pushed onto elder residents, presented as a prerequisite for admittance into long term care nursing homes. Of particular concern to arbitration agreements in this setting, is the lack of fair bargaining power. Most elderly residents do not have assistance when reviewing their intake documents. So, when they are presented with an arbitration agreement, they will blindly sign it, unaware that they have signed away their right to appeal or their 7th Amendment right to a jury. Many agreements are presented in a "take it or leave it" setting, creating pressure and stress. And, many signed arbitration agreements stipulate that the nursing home gets to choose the arbitrator who tends to render decisions in favor of the nursing home because they want the repeat business. Arbitration leads to many biased decisions and lower awards granted to plaintiffs. A 2009 study commissioned by the American Health Care Association, which represents more than 13,400 nursing homes, found the average award after arbitration was 35% lower than if the plaintiff had gone to court. (1) To make matters worse, arbitrations are not on the public record, meaning that whatever negligence or abuse went on within the nursing home can be shielded from the public.

According to Marco Quintanar, Program Supervisor at the Long Term Care Ombudsman Services of Santa Barbara County, nursing homes are overwhelmed and understaffed due to the generation of baby boomer residents who are reaching retirement and needing long term care. Quintanar referred to this as the "Silver Hurricane" and stated that in the U.S. an average of 10,000 people a day are turning 65 or older. Many nurses have an overloaded schedule of residents to care for, they lack sufficient training and many homes are cutting high costs by hiring less staff. (2) As nursing homes hit their resident capacity, many problems surface, causing an abundance of potential lawsuits. In fact, in a detailed study reviewing the statistics of California residents who died in nursing homes, it was found that more than half of the residents had received unacceptable care, including neglect, failure to properly treat, and failure to manage pain. (3)

Nicole Hornick

When an elder resident signs an arbitration agreement as a part of their admission, it creates a huge burden for that elder or their loved ones to litigate any potential claim of neglect or abuse, and most times the outcome will not be in their favor. Elders and family members should be educated of the risks surrounding arbitration. In fact, most elder law advocates urge people to refrain from signing them at all. (4)

What Is Being Done

Just as recently as this past September, the National Academy of Elder Law Attorneys (NAELA) successfully advocated the Center of Medicaid and Medicare Services (CMS) to ban federal funding to long-term care facilities that require residents to sign arbitration agreements before a dispute arises. (5) More than 15,000 long-term care facilities participate in the Medicare and Medicaid programs, which controls more than a $1 trillion dollars in federal spending will be affected.

Further action towards limiting pre-admission arbitration agreements in nursing homes was provided by the California Health and Safety Codes. Under Health and Safety Code §1599.81(a), nursing homes can no longer require applicants to sign arbitration agreements as a condition of admission or of medical treatment. This means that nursing homes cannot refuse to admit a patient who has not or will not sign the contract. Nonetheless, residents still sign them. As is repeatedly stated on the California Advocates for Nursing Home Reform (CANHR) website, the best advice to clients is, "Don't sign them!"

Furthermore, California Health & Safety Codes §§ 1430(b) & 1599.81(d)) state an arbitration agreement must be on a form separate from the admission agreement and must have a separate signature. And in the event the admission contract contains an arbitration clause, the patient may not waive his or her ability to sue for violation of the Patient's Bill of Rights. A Patient's Bill of Rights are rights guaranteed to patients regarding patient information, fair treatment and autonomy over medical decisions. (6) So, if an elder claims their Patient's Rights have been violated, they are not bound by an arbitration agreement and may take their matter to a public court. And finally, according to California Code of Civil Procedure § 1295(c), a resident can rescind any signed arbitration agreement presented by the nursing home by giving written notice to the nursing home within 30 days of their initial signing of the agreement. To put it simply, California's response is: Do not sign them, but if you do, we will give you 30 days to change your mind.

Unfortunately, the Federal Government does not see eye to eye with California. The FAA preempts state law and allows the arbitration agreement to survive state scrutiny. The US Supreme Court ruled in 2011 that "when state law prohibits outright the arbitration of a particular type of claim, the analysis is straightforward: The conflicting rule is displaced by the FAA." (7) So in essence, the FAA prohibits states from banning the use of arbitration agreements, whether or not arbitration is preferred by that state.

However, thanks to the creative loopholes of our law, clever attorneys have still managed to challenge the validity of the agreements through standard contract defenses. These defenses might be the key to protecting our elder's rights and we, as attorneys, should encourage them to try their claim in the public court system.

Lack of Capacity

Formation of a valid contract requires a meeting of the minds. Usually an elder who has recently suffered a stroke, or has some other physical or mental trauma may lack the legal capacity required to assent to a contract. Make sure to always assess and evaluate an elder's mental awareness.

Lack of Authority

Many times a friend or family member will sign the admittance documents and arbitration agreement when the elder cannot do so for themselves. Whether or not this is a valid formation of a contract depends on whether the person signing on behalf of the resident had actual authority to do so. "The strong public policy in favor of arbitration does not extend to those who are not parties to an arbitration agreement, and a party cannot be compelled to arbitrate a dispute that he has not agreed to resolve by arbitration. There are three exceptions to the rule: (1) 'an agent can bind a principal,' (2) 'spouses can bind each other,' and (3) 'a parent can bind a minor child.'" (8) Make sure to review the signature of the agreement and determine whether that person had actual authority to sign on the elder's behalf.

Unconscionable

Remember, courts may exercise discretion as to whether the contract was unconscionable, but always check the agreement's terms and the situation in which it was presented. In *Doctor's Associates, Inc. v. Casarotto,* the court noted that "generally applicable contract defenses, such as fraud, duress, or unconsionability, may be applied to invalidate arbitration agreements…" (9)

FAA not Applicable.

According to *Daniels v. Sunrise Senior Living, Inc.*, Daniels, the aggrieved daughter of a senior mother, was able to pursue a claim of wrongful death against the nursing home despite her mother having signed an arbitration agreement. The court found that even though her mother was subject to the arbitration agreement, "Daniel's wrongful death claim is personal to her and lies independent of the survivor's claim." (10) Therefore residents cannot waive the right of survivors to pursue a wrongful death claim against an assisted living facility.

Arbitration Agreements in nursing homes pose a problem to elder citizens. Further, they impede on rights guaranteed in our Constitution. Arbitrations, in reality, often only benefit nursing homes. We tend to forget that nursing homes are a business, and although safety is a main concern, nursing homes need to make a profit. Mistakes happen, elders are vulnerable and lives are put at risk. Nursing homes should not need to seek protections from lawsuits. They should be held to a high standard of care as reasonable professionals, and when their care falls below that standard they should be held accountable. Most of us will one day be in a situation where we need long term care assistance and so it should be our imperative to make sure mistakes get noticed, problems get fixed and justice prevails. ■

Nicole Hornick is a fourth year law student at Santa Barbara Colleges of Law and will be taking the July 2017 Bar. She is currently a paralegal at Loskamp and Wohlgemuth (www.lw-lawoffices.com).

ENDNOTES

1. The American Health Care Association Special Study on Arbitra-

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Stairway to Infringement: Copyright Issues in Popular Songs

By Bruce McIver

It has come to my attention that if we think the wars over copyright infringement are settled, we may be whistling Dixie. In the contemporary arena of music, copyright infringement poses some new and interesting issues.

The protections afforded authors and inventors by copyright, patents, and other intellectual property derive, as we know, from Article I, Section 8 [8] of the Constitution and are codified in, among others, the Copyright Act of 1976. Various international conventions and treaties expand those rights on a global scale.

Three notable cases of infringement, the holdings of the court, and the questions these cases raise deserve attention.

First is the case of *Bright Tunes Music v. Harrisongs Music 420 F. Supp. 177 (S.D.N.Y. 1976*. George Harrison's "My Sweet Lord" became a smash hit in 1970, rising to number one on the popular music charts. What George didn't realize was that he misappropriated the melody and harmony, almost verbatim, from a 1962 hit song by The Chiffons: "He's So Fine." The court held that George was aware of "He's So Fine" and that he subconsciously cribbed the melodies, harmonies, and even a grace note in precisely the same position in both songs. The case dragged on for years, with complications created by the bankruptcy of Bright Tunes and breach of fiduciary duty by the Beatles former manager, Allen Klein. The case was settled finally for a dollar amount of one and a half million dollars, later cut in half, as well as much heartache. A comparison of the two songs is available on the website sponsored by Columbia Law School and the USC Gould School of Law (mcir.usc.edu). So the reader may judge for herself.

Second is the Australian case of *EMI Songs Australia Pty Limited & Anor v Larrikin Music Publishing Pty Ltd* [2011] HCATrans 284. Larrikin Music filed suit after hearing about a 2007 TV show in which the question was asked--what children's song is echoed in the flute riff of Men at Work's "Down Under"? The answer given was the well-known children's song "Kookaburra." The High Court of Australia upheld the lower court decision that the iconic flute riffs of the 1980's hit "Down Under" by Men At Work infringed the copyright of the children's song "Kookaburra Sits in the Old Gumtree" written by Marion Sinclair in 1934. The decision focused narrowly on two contentious bars of Kookaburra and the flute riffs, but not the two songs as a whole. The Australian Court found that "Down Under" copied a "substantial part" of Kookaburra and that defendant EMI misrepresented its entitlement to 100% of the royalties. This was a particularly painful case for the musicians of Men at Work: in the aftermath of the litigation, Greg Ham, who played the flute riff, and the father of Colin Hay, who wrote it, died, both deaths arising allegedly from the stress of the litigation.

Bruce McIver

Last is the case in Federal District Court in Los Angeles, now under appeal, concerning the iconic opening riff of Led Zeppelin's "Stairway to Heaven" from1971 and an instrumental piece "Taurus" from 1966 by the band Spirit. A comparison by listening to the two pieces suggests that there may have been a borrowing, subconscious perhaps as in the George Harrison case, or even conscious. (To listen to Spirit's "Taurus" for comparision, the reader should google: "spirit taurus youtube".) Led Zeppelin knew of the band Spirit, covered another song by Spirit, and played in successive concerts with Spirit on their first American tour. However, in *Skidmore v Zeppelin (Case 2:14-cv-03089-JS Document 1 Filed 05/31/14)* Federal Judge R. Gary Klausner barred the jury from hearing Spirit's recorded version of "Taurus" since copyright of the song extended only to the sheet music. All the jury was permitted to hear was a professional musician's rendition of the sheet music. This was a fatal blow to the case. Led Zeppelin was denied recouping from Spirit its legal fees, and the estate of the song's composer, Randy Wolfe (AKA Randy California), who died in 1997, is appealing.

So what do these three cases tell us? Well, the first two plaintiffs were successful, while the third, Skidmore, was unsuccessful at the Federal District Level. An appeal is apparently in the works in Skidmore. It is difficult to discuss trends in copyright litigation. Led Zeppelin succeeded, in my opinion, because the judge barred the jury from listening to the recorded version of Spirit's "Taurus," which could

have been persuasive. Many who have compared them would agree. It is possible that a holder of a sound recording copyright, if any, rather than the sheet music copyright, could have filed suit and produced a different result.[1]

The question concerning the current situation as reflected in these cases is whether copyright law is actually affording the protections that the Constitution guarantees. Article 1.8.8 states: "Congress shall have the power to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries." Are these guarantees encouraging creativity in music or discouraging creativity with the paralyzing emphasis on infringement?

Added to the fray is the recent infringement case regarding the pop 2013 tune "Blurred Lines" by Robin Thicke and Pharrell Williams. Some melodic lines of Marvin Gaye's 1977 hit "Got To Give It Up" were adjudged substantially similar to those of "Blurred Lines." Interestingly, the judge in this case, as in "Stairway," did not allow the Marvin Gaye song to be played in court for comparison; only the sheet music was admitted as evidence. But the judgment reversed that of the "Stairway" case.

When Andrew Lloyd Weber came up with the core melody for "Memory" in *Cats*, he feared that it was too similar to the theme of Bolero and the flute solo in "California Dreamin'" by the Mamas and the Papas. When he asked his father what it sounded like, his father replied: "like a million dollars." Webber was not sued for infringement.

But in today's musical environment, with recorded songs universally accessible, and the chances of unintended and subconscious influence are infinitely magnified, Webber was justifiably cautious about "Memory." In a situation like that of George Harrison or Men at Work, where the infringement was more than likely unintentional, the law does not recognize the distinction between intentional infringement and subconscious appropriation. Damages may differ but the judgment is the same.

Further problematic are cases of sampling, wherein one song samples a phrase or bar of a copyrighted song in a "substantial part.'' This is a judgment call since there is no hard and fast "number of notes" rule; the test is whether the songs are "substantially similar."[2] ("Substantial similarity" and "striking similarity" are key terms in testing for infringement in music generally.) Even if the songwriter gets permission for the sampled phrase and pays the licensing fee, the song sampled may itself have samples of other songs for which permission would be required.

Now, is Andrew Lloyd Webber's fear of infringement conducive to promoting the useful arts or, rather, discouraging them? Is it making criminals of songwriters as well as other producers of the useful arts? Well, possibly so. The composer Stravinsky was reputed to have said, *"A good composer does not imitate; he steals."* To which one might add, "and gets away with it (sometimes)." Variations of this aphorism have been attributed to, among others, T. S. Eliot, Pablo Picasso, and Steve Jobs! Aaron Copeland in *Appalachian Spring* definitely "stole" the melody and harmony of Joseph Brackett's "Simple Gifts," but by 1944 when Copeland's ballet was first performed, "Simple Gifts" (written in 1848) was thankfully long out of copyright. Must composers wait that long?

In the case of *Skidmore v Led Zeppelin*, I think the outcome may have been different if the jury had been permitted to listen to the recorded version of Spirit's "Taurus," rather than a mechanical reproduction of the notes from the sheet music. Moreover, Spirit performed "Taurus" many times in concerts where Led Zepelin shared the stage. Zepelin had a copy of the Spirit album and covered a Spirit song on the flip side of the album. It is clear that they knew of the song, but if proven to be an infringement, whether it was a conscious appropriation or an intentional one will remain indeterminate. In the interest of promoting the useful arts, and not discouraging them, this question is worth bearing in mind in the analysis of copyright infringement cases involving music. ■

ENDNOTES

1 "Congress did not extend federal copyright protection to sound recordings until the Sound Recording Act of 1971 . . . and then only to sound recordings fixed after February 15, 1972." *Michael Skidmore v. Led Zeppelin et al.* CV 15-3462 RGK (AGRx), page 15.

2 See the discussion of "substantial similarity," page 15, in *Michael Skidmore v. Led Zeppelin et. al., Case No.* CV 15-3462 RGK (AGRx) available on line at: https://assets.documentcloud.org/documents/2799929/Led-Judge-Ruling.pdf

Bruce McIver began practicing law in Santa Barbara in 2004 after graduating from the Santa Barbara College of Law. He volunteers regularly as a Teen Court Judge and with Partners in Education. In 1974 he received a Ph.D. in English from UCSB and, over a span of 30 years, taught literature and writing courses at Reed College, UCLA, UCSB, University of Kent at Canterbury, University of Ljubljana, and Union College. His published works include writings on Shakespeare, Hemingway, Malamud, Tobias Wolff, John Earle, and Sir Thomas Overbury. More than a dozen of his short pieces on literature and law and other topics have appeared in previous issues the Santa Barbara Lawyer *magazine. He is married with two children and three grandchildren.*

Why Do So Few Lawyers Handle Federal Workers' Compensation Cases?

By Michael P. McCready

A new client calls your office. He explains how he was injured on the job. You figure, "great, a new worker's compensation case!" After listening further, the client tells you he works for the US Postal Service. A federal employee. You immediately stop the conversation and tell the client you don't handle federal workers' compensation cases, and what's more, you don't know anyone who does. The client hangs up and is left on his own.

But why is it that so few lawyers handle federal workers' compensation cases? There are 2.1 million federal civilian employees. That is a huge potential client base, larger than the working age population of twenty states! There are no court appearances in federal workers' compensation cases. All proceedings are done telephonically and almost all documents are uploaded electronically. Because it is based on federal law, you can represent clients all over the country, and in fact, all over the world. There are no state restrictions to practicing law with federal workers' compensation cases. Finally, many federal agencies are at a high risk of sustaining work related injuries. Employees of such federal agencies as the United States Postal Service (USPS), the Veterans Health Administration (VA), the Transportation Security Administration (TSA) and the Department of Homeland Security (DHS) are all covered under federal workers' compensation. Given these factors, there should be a lot of lawyers who handle federal workers' compensation cases. But there aren't. Why?

First, there are no contingency fees in federal workers' compensation. In fact, federal law makes it a misdemeanor to charge an injured federal worker a contingency fee. Therefore, all work for federal employees must be billed by the hour with detailed descriptions of the work performed and the time spent. Traditional workers' compensation and personal injury lawyers are not accustomed to keeping track of time and billing clients. Additionally, contingency lawyers will charge a percentage of the recovery, which is forbidden in federal cases.

Second, although being able to represent clients nationwide is a positive, when it comes to collecting an unpaid fee for work performed, it is a serious limitation. You can't be suing people all over the country who do not pay your fee. For this reason, most federal workers' compensation lawyers charge an upfront retainer. Imagine being injured on the job, perhaps not being paid, and having to send a retainer to a lawyer to represent you in a workers' compensation case. The contingency tort system is designed to allow everyone access to the courthouse, regardless of economic means. In federal workers' compensation cases, only those who pay their lawyer have representation.

Michael P. McCready

Third, assume a client has paid a retainer and you have kept detailed billing records. You are not allowed to transfer the retainer to your operating account until the client has approved the bill. Yes, that's right, you don't get paid if the client disapproves of the bill, even if you do the work. In a contingency case, you take the risk that you may not win, and if a contingency lawyer fails to make a recovery, there is no fee. In federal workers' compensation, you can do the work, and win or lose, you may not get paid if a client does not approve of your fee.

Fourth, any compensation received by an injured federal employee is sent directly to the worker, not his or her attorney. In traditional contingency fee practice, you immediately send a notice of attorney lien or letter of representation to protect your right to get paid. Usually, the settlement check is made payable to the lawyer and the client. Not in federal workers' compensation cases. The check is made payable to the client and mailed directly to the client. As you can imagine, this severely hampers a lawyer's ability to get paid, and reinforces the need for a retainer. Because the check is mailed to the client, case loan companies will not provide a case advance to pay a retainer.

It should be obvious from the above discussion of federal workers' compensation why there are so few lawyers handling these cases. The federal government justifies these procedures by proclaiming they want the injured worker to receive as much of the recovery as possible, not an attorney. The prohibition against contingency fees is also meant to protect federal employees from being "overcharged" for legal services. The assurance that attorneys' fees and the claimant's recovery are kept separate is part of that protec-

tion. But, what they have done is essentially cut lawyers out of the federal system and deprived federal workers the ability to have legal representation for their injuries.

Setting aside the ability of the lawyer to get paid, the federal workers' compensation system is quite similar to state workers' compensation systems. Like state Workers' Compensation Commissions, in the federal system, "[t]he Office of Workers' Compensation Programs administers disability compensation programs which provide wage replacement benefits, medical treatment, vocational rehabilitation, and other benefits to certain employees who experience work-related injury or occupational disease."

Claims must be filed timely and injuries must arise within the performance of duty. There must be a factual basis to the claim as well as a medical basis. Finally, there must be a causal connection between the work and the injury. The injured federal worker has the burden of proof on each of these elements. Federal law covers both traumatic injuries as well as occupational illness which occurs over time, such as toxic exposure and repetitive injuries.

Injured federal employees are also entitled to a Schedule Award for certain permanent medical impairments. OWCP uses the *AMA Guides to the Evaluation of Permanent Impairment, 6th Edition* exclusively. When an injured federal worker reaches maximum medical improvement, he or she can obtain an impairment rating which will serve as the basis of their Schedule Award. This is the same as many state workers' compensation systems, while other state systems allow for a variety of factors to determine the level of permanent impairment.

Unfortunately, there is no entitlement to a Schedule Award under federal law for mental conditions nor for injuries to the head, brain or back. Many state workers' compensation systems cover these injuries as "person as a whole" or "non-scheduled injuries," but under some states' systems as well as the federal system, injuries to these body parts do not entitle an injured worker to a scheduled award. However, if an injury to the head, brain or back causes permanent impairment to an extremity (arm or leg, for example), the injured worker may be entitled to a Schedule Award for that region or body part. A Schedule Award is calculated using a formula which includes the AMA impairment rating and the rate of pay of the injured federal employee. Scheduled Awards are paid over a period of weeks, except in exceptional circumstances where it can be paid in a lump sum.

One significant difference between state and federal workers' compensation systems is the role of neutral adjudicator. Under state law, there is typically a neutral arbitrator or commissioner who decides disputed issues and has the authority to enter an award for a compensable injury. A claims adjuster and/or respondent's attorney are paid by an employer or insurance company and are adversarial to the interests of an injured worker. The OWCP employs claims examiners. A claims examiner is an adjuster and arbitrator rolled into one. The claims examiner deals directly with the injured worker like an adjuster. But the claims examiner also has the authority to determine compensability, benefits and ultimately the amount of the award. If you are unhappy with a decision of an OWCP claims examiner, your remedy is to file an appeal.

In the statute which creates the federal workers' compensation system, it explicitly states the system is meant to be non-adversarial. "The mission of the OWCP is to protect the interests of workers who are injured or become ill on the job, their families and their employers by making timely, appropriate and accurate decisions on claims, providing prompt payment of benefits and helping the injured worker return to gainful employment as early as is feasible." State workers' compensation systems typically have similar such platitudes. But, state workers' compensation systems are premised on an adversarial model, with neutral adjudicators. The federal system is not, and thus, the dual role of claims examiner.

As a practical matter, an injured federal worker is at the mercy of a claims examiner, with an appeal being the only remedy for a disagreement with their determination. Appeals are governed by rigid procedural rules and take a long time to be resolved. In the case of an adverse determination by a claims examiner, his or her decision is often the final word. Compound this with the fact that most injured federal employees proceed *pro se* and you can imagine the scale of the injustice.

While a claim may be denied by OWCP for factual or jurisdictional reasons, most claims fail because the medical records of the treating physician do not satisfy the causation element of the claim. To have a claim approved by OWCP, there must be adequate medical documentation. Medical records must describe in detail the employment incident or circumstance that resulted in the injury, whether traumatic or occupational. Generalizations such as, "hurt at work" are inadequate. The treating doctor must provide a firm diagnosis of the injury: a herniated C5-C6 disc, a torn knee ligament, asthma, etc. A diagnosis of back pain is not sufficient. Medical records must offer an opinion on the causal relationship between the injury and the disability or need for medical treatment. Furthermore, claims examiners are now asking for an explanation of how the job duty caused the injury or the case will be denied. Although not necessary for medical treatment, a medical record must

clearly indicate the doctor's opinion as to the relationship between the injury and the medical treatment in order to be approved by OWCP. A doctor's opinions and conclusions on a causal relationship must be supported with reasoned analysis and objective findings. Once again, not typically included in a doctor's medical records, but for treatment to be approved by OWCP, a doctor must justify his or her opinions in the medical record itself or separate narrative.

A doctor must conclude that his or her opinions are to a "reasonable degree of medical certainty" basis. A doctor does not need to know definitively that a medical condition was related to work, just that it is more likely than not the result of a work related injury or condition. A doctor's opinion should never be equivocal. He or she should not use terms such as "appears" or "might be" or "likely." These words do not meet the more probable than not basis and will result in a denial of the injured worker's claim. We always advise doctors to include the following magic words in their medical records: "it is my opinion that to a reasonable degree of medical certainty that the (describe medical condition) was caused/aggravated/accelerated by (describe work injury)."

There are several types of causes of medical conditions which can be covered under federal workers' compensation coverage. A *direct* causation relationship is demonstrated when the injury or factors of employment, through a natural and unbroken sequence, result in the condition claimed. This is the simplest causation and usually results from one, single traumatic event. An *aggravation* relationship occurs if a pre-existing condition worsens, either temporarily or permanently, by an injury arising in the course of employment. This is true even if the aggravation is only 1% from work duties. A new trauma or employment related injury may aggravate a pre-existing degenerative process, and coverage by OWCP would last for the duration of the aggravation as medically determined. A *temporary aggravation* involves a limited period of medical treatment and/or disability, after which the employee returns to his previous physical or mental status. Compensation from OWCP is payable only for the period of aggravation established by the weight of medical evidence and not for any disability caused by the underlying disease. This is true even if the patient cannot return to the job held at the time of the injury because the pre-existing condition may worsen if he does return. A *permanent aggravation* occurs when a condition will persist indefinitely due to the effects of employment related injury or when a condition is materially worsened such that it will not revert to its previous level of severity. An employment related injury or disease qualifies as an *acceleration* if it hastens the development of an underlying condition, and the acceleration is said to occur when the ordinary course of the disease does not account for the speed with which a condition develops. Finally, a *latent condition* that would not have manifested itself but for the employment is said to have been precipitated by the factors of employment.

Federal workers' compensation law is governed by several sources. The Department of Labor is responsible for administering workers' compensation claims for employees of the federal government. The Department of Labor exercises this responsibility through its Office of Workers' Compensation Programs ("OWCP"), which is responsible for the initial processing of claims, and through the Employees' Compensation Appeals Board ("ECAB"), which is responsible for appellate review of workers' compensation claim decisions by OWCP. The Department of Labor derives its authority and jurisdiction over federal sector workers' compensation claims from the Federal Employees' Compensation Act ("FECA").

FECA, codified at 5 USC § 8101 et seq., is a complex statutory scheme that provides for the payment of workers' compensation benefits to civilian officers and employees of all branches of the U.S. government and individuals employed by the District of Columbia. FECA provides for the payment of compensation for wage loss and for certain permanent bodily impairments incurred by employees as a result of injury, illness or death sustained while in the performance of their duties. In addition to financial compensation, employees may receive reasonable medical and related services. Like state workers' compensation systems, FECA is the exclusive remedy for federal employees who are injured on the job. 5 USC § 8116(c).

Although federal workers' compensation law has many similarities to its state counterparts, the role of the injured worker's attorney is quite different. The vast number of injured federal workers either can't afford to hire a federal worker's compensation lawyer or don't see the value in paying a lawyer a retainer. Many potential clients are surprised we cannot charge a contingency fee and shocked that they have to pay an attorney themselves. In our practice, only one in ten injured federal employees who contact our office retain us for representation. If federal compensation lawyers were able to charge a contingency fee and have the check mailed to their office, that number would be closer to nine in ten.

It's a very sad system and it is heart-breaking to hear the stories of these workers. Too often, people come to us because they tried to appeal it on their own and now are losing their house because they have gone so long without

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Shakespeare's Best Advice

By Justice William W. Bedsworth

"Writing . . . is a horrible, exhausting struggle, like a bout of some painful illness. One would never undertake such a thing if one were not driven by some demon whom one can neither resist nor understand." That's George Orwell.

"I've never written easily: most of the time I detest the process." That's Leonard Cohen.

"People write for the same reason they climb mountains. And neither writers nor mountain climbers can explain it." That's me.

I've written—or edited—professionally since I was nineteen.[1] My entire career—once I figured out I was miscast as a trial lawyer—has been based on writing. And I have never once—ever—sat down to write without a feeling of overweening dread.

You know that feeling. It's time to write the summary judgment motion or the 1538.5 or the Respondent's Brief and you spend three days in a blue funk, unable to figure out why you feel so bad until you remember, "Oh yeah, Saturday I have to write that thing."

And you have to write it Saturday because you've put it off until the last possible minute. People are impressed that you have taken care of so many other long overdue tasks; they don't recognize it as a frenzied and desperate effort to do *anything* rather than sit down to write.

"Jack, I understand you built a new garage this weekend even though it was snowing and you were passing a kidney stone. That's pretty impressive."

"Yeah, well it was that or write the motions *in limine*."

No one really likes to write. It's too personal. It's like opening an artery and hoping people approve of the color of your blood and don't think you made too much of a mess displaying it.

But some of us *need* to write. It's a virus—some weird intellectual Huntington's Chorea thing that lurks in the darker recesses of your being until you're having too much fun to consider suicide and then bursts forth, overwhelms your defenses, and turns you into a bot.

That happened to me in high school, and once it happens, you write because you have to. You need to. Resistance is futile; you'd have a better chance against the Borg.

So here I am, in the thirty-sixth year of writing this column, my twentieth year of writing appellate opinions, and I still approach the keyboard wondering how many arteries I will have to open and whether we couldn't use a new garage.

But most of you write not because of some sinister chromosomal deficiency but because your job requires it. Most of you are going to bang out that brief—painful as it is—and then spend an hour or two brainstorming all the different things you might do to make sure you never have to go through that again. Settle more cases, hire an associate, leave the practice and start building garages . . . whatever it takes.

For most of you, that writing task was a hurdle that had to be negotiated, and now you can go back to the parts of the steeplechase that you enjoy. And you can do so, secure in the knowledge that I must be every bit as mentally deficient as you assumed or I could have found a job that didn't require me to write on a daily basis.

But it's you I want to address. Not the people like me, who have a creative urge and no other talent;[2] we're pretty much unsaveable. The rest of you . . . well, there's probably still hope for you.

This has been a long-winded preamble[3] to what I want to say today. What I want to say is only tangentially related to the pain and suffering caused by writing, but it's writing that brought it to mind. Specifically, bad writing.

More specifically, the exchange between a couple of lawyers in Ohio that was precipitated by bad writing.

Timothy Chappars and Nicholas Subashi have been on opposite sides of the counsel table for many years. Chappars is a personal injury lawyer and Subashi handles insurance defense.

Subashi filed an answer to one of Chappar's complaints that included a Motion to Strike. The motion to strike said:

SIXTEENTH DEFENSE

Answering Defendant alleges that the Plaintiffs' Complaint, by containing run-on sentences, multiple allegations in the same paragraph, conclusions, verbose exaggerations, and "stream of consciousness" rhetoric, violates rule 8 of the Ohio Rules of Civil Procedure and should, therefore, be stricken in its entirety.

Whoaaa! Talk about a shot across the bow! Run-on sentences and "excess verbosity" are bases for dismissal of counts in Ohio!? Sounds like a jurisdiction I oughta be

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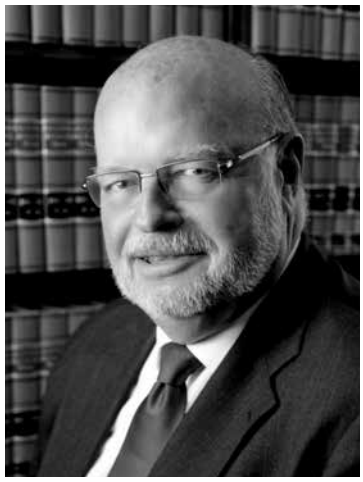
Immunity Requests and Grants

By Robert Sanger[1]



Robert Sanger

There is much discussion, as this is being written, about immunity requests and grants. This is a subject that not only affects national politics but is a fact of life in corporate America. Proffer agreements, deferred prosecution agreements, cooperation agreements and actual grants of immunity represent a dangerous and sometimes unseemly side of the legal system.

In this month's *Criminal Justice* column, we will look at the practical side of immunity arrangements. Although they pose dangers and are sometimes unseemly, they are procedures that are available and that have to be discussed with the client in appropriate circumstances. We will do a horseback view of these procedures primarily as applicable in white collar federal cases ranging from fraud to public corruption with a brief nod to the application of the system to the national political scene.

Witness, Subject and Target

When a federal law enforcement agent contacts a person, they generally have an idea as to whether the person is a witness, a subject or a target. In white collar cases this distinction is sometimes hard to predict. In a typical street crime, say a car-jacking, the unrelated bystander who comes out of the store after shopping and sees a suspect yank a driver out of a car in the parking lot is pretty reliably just a witness. There are those cases, of course, where the bystander turns out to actually be in on it but, in the typical case, the bystander is truly just a witness.

In white-collar cases, however, the distinction is often harder to make. A person who witnesses something relating to, say, a financial transaction or a series of complex political negotiations may be involved in the transaction or negotiations themselves. Therefore, witnesses cannot always be sure whether their activities in a transaction or negotiation could be considered to be acts in furtherance of a scheme, which, if done with knowledge and intent, could make the person a conspirator or a principal by virtue of aiding and abetting. In crimes of government corruption or violations of criminal restrictions on the behavior of government officials, a meeting or seemingly innocent correspondence could well be construed as criminal.

Furthermore, the client is not always going to be the best source of information on this subject. People may be unwittingly involved and be convinced that they did nothing wrong. However, the government agents and prosecutors (AUSAs) may think otherwise. Being indicted in a federal criminal case can be extremely expensive and can ruin an individual financially and personally even if the individual is eventually exonerated. Many businesses have been reduced to bankruptcy or abandonment following indictment even if no conviction was ever obtained. Therefore, it is a big decision, for which the individual client may be ill-equipped, to conclude that he or she is merely a witness.

One key for lawyers--business, corporate and criminal--is to make sure that their business clients know that, if they are confronted by federal law enforcement agents, they have the right (absent a life-threatening emergency – e.g., if the building is on fire, tell them where the people are inside) to not speak to the agents without talking to their own lawyer. Furthermore, if the client hears of any government activity, such as vendors or business associates being asked questions about the client, subpoenas being served on banks and the like, clients should know to immediately tell their lawyer so that the lawyer can find out who the agent is and what AUSA, if any, is on the case. Again, one of the fundamental questions is whether the client is a witness, a subject or a target. Until that is established, the client has the right to remain silent and needs to insist on that right.

If the attorney can establish a working relationship with the agents and the AUSA, they will usually tell the attorney if the client is a witness, subject or target. This becomes a bit tricky. Most federal agents and AUSA's will be pretty straightforward in telling a lawyer if they believe that the client is only a witness. However, they will always hedge their bets and say something ominous like, "Based on the information we have at this point." The tension for the lawyer is that, if the client is truly just a witness and has no complicity or conspiratorial involvement, the client can probably cement the witness status by cooperating

fully. While it is beyond the scope of this article, there are also situations in corporate internal investigations where substantial corporate assets may also be on the line based on cooperation. Thus, in the simple case that is more akin to the bystander coming out into the parking lot after shopping--if there is one in the white collar world—it may be good for the client to answer the questions and let law enforcement do its work.

The risk in all of this is that law enforcement or the AUSA may develop other information or theories, of which the lawyer or the client is not aware, that rightly or wrongly implicates the client as a conspirator or principal in the scheme. Rightly or wrongly, that may elevate the witness to a subject or a target. A subject is a person who the agents and AUSA are considering as a possible target. The target is the person (or group of people) who are the intended defendants in a pending or potential grand jury indictment. If a person is a subject or a target, then such person should not have any communication with the agents or AUSA or anyone else except the person's lawyer.

The old wisdom among criminal defense lawyers is that the lawyers should all stand together and stand tall; the clients should remain silent; and the government should be put to its proof. There is much to be said for that. One of the dangerous and unseemly aspects of cooperation is that the government can just sit back and watch as a bunch of terrified people run around doing everything they can to get everyone else convicted to save themselves. False evidence, exaggerated allegations and outright wrongful convictions can come from this. On the other hand, the government sees this as a powerful tool. The Big Brother aspect of cooperation cannot be denied and yet lawyers have to inform clients of the possible benefits. This is an age of mass incarceration where being indicted alone can ruin a person but being convicted can result in sentences that are life ending. This makes for tough choices.

Immunity

At the outset, it should be understood that a formal grant of immunity can only be made by a court.[2] The government has to go before a judge and apply for an order of limited immunity in judicial, administrative and congressional proceedings and that is available only if the client asserts a Fifth Amendment privilege. This usually occurs where a witness has been subpoenaed before the Grand Jury and takes the Fifth. The AUSA concludes that the government would rather have the testimony than prosecute the witness. Therefore, they go to the Duty Judge[3] and seek an order. That order would grant use immunity only.

It is also possible for an AUSA to agree to informal immunity. That is generally an agreement that often will only bind the prosecutors in the particular federal district although a commitment from Main Justice can bind the Department of Justice as a whole. There are also possible consequences of informal grants that can affect prosecutions on a case-by-case basis based on constitutional principles.[4] However, for the sake of this article, suffice it to say that there are various types of immunity, including use immunity, derivative use immunity and transactional immunity. Use immunity, the most popular, simply means that the government cannot use anything said by the cooperating client in their case in chief if they do proceed against the client. They can use it to impeach the client if the client testifies and, in some cases, can use it in the event the client's counsel pursues certain lines of questioning in cross-examination. Derivative use immunity means that the government cannot use information derived from information given by the client – which can lead to a labyrinth of pretrial orders. And, of course, transactional immunity is the best protection for the client. If the client talks about a crime the client can no longer be prosecuted for that crime.

Proffers

Clients who are potential subjects or targets, especially those who might be facing indictment for serious involvement in criminal activity, will want to have transactional immunity if they are going to cooperate at all. If they cannot get that, they want to have the broadest possible grant of immunity that their lawyers can negotiate. Of course, the government does not want to grant anything that will undermine the value of the client as a witness. They would rather have the client testify without any promises at all. In addition, the government does not want to buy a pig in a poke – they want to know what they are getting before they agree to give the client any benefits. This, unfortunately, leads to misunderstandings and mistaken expectations. It also may lead to Brady violations where a wink and a nod or an even more formal agreement to give the client benefits is not disclosed to a defendant who is eventually prosecuted based on the client's testimony.

A partial way around some of these problems is for a proffer. That usually proceeds by way of an informal approach by the lawyer inquiring "hypothetically" what the reaction of the government would be if "hypothetically" the client were to be able to give some information. If there is interest, then the government might offer a "Queen for a Day" letter that broadly outlines a weak form of use immunity in exchange for the client sitting down with them and talking. There may be some ability to negotiate terms in this proffer letter and, ideally, to negotiate the ultimate terms

of the benefits agreement if the client testifies. Eventually, if the proffer agreement is made, the client will meet with the AUSA, one or more special agents, and, in technical cases, sometimes professionals assisting the government such as accountants or experts. The lawyer is present and can intercede if things go off track but, generally, if a client is going to do this, the client needs to know that he or she has to lay everything out truthfully – and if the client does not want to make that commitment, then the client should return to the protection of the right to remain silent and not make a proffer.

Often the government will not want to make specific benefits commitments in writing but will strongly suggest that there may be benefits if the proffer goes well and if the client agrees to testify truthfully before the Grand Jury or at trial. In the case against the target, the government does not want to compromise the effectiveness of the witness by having made a specific agreement. On the other hand, the lawyer for the client who is proffering wants to have a specific agreement as to the benefits the client will receive. From the lawyer's standpoint, the best practice is to get a clear written agreement, for instance, that there will be no prosecution of the client at all and that, say, the client will be relocated. But this does not always work and the client should be reminded that cooperation is a choice.

Conclusion

The agents and AUSAs do not generally want to commit to a benefits agreement and, generally, will not apply for formal judicial immunity unless and until there is an assertion of the Fifth Amendment privilege. There are clients who will panic unnecessarily or, perhaps, because they are accurately seeing the handwriting on the wall. They may want to run in and get immunity and agree to testify. As described above, on the one hand, the government loves to have people come in and spill the beans; on the other hand, they are not likely at an early stage to grant anything but a "Queen for a Day" to get a proffer.

Certainly, in high profile cases with a lot at stake, the lawyer may be doing the client a good service to tie down an immunity deal early. Prosecutors often say that the first person on the boat gets the best deal. But, even in high profile cases, AUSAs and agents will generally want to really know what they are getting into and, for instance, whether the client's story would be corroborated. They also want to evaluate whether they are giving up a big fish in order to get the goods on a smaller fish or whether the client's information will take them to a bigger fish. Other than a weak "Queen for a Day," prosecutors want to know that they are "buying the right testimony" before an actual benefits/immunity package is agreed upon.

Of course, high profile cases that are larger than life cause people to think larger than life. This manifests itself in prosecutors, judges, defense lawyers and public officials making decisions that they would not make in the normal course of things. Particularly, where there are some fairly historic national consequences, just as one would hope there would be measured and thoughtful decisions, there are likely to be some that are not. It will be interesting to see what high profile immunity grants are given, under what conditions and when. Will the system be compromised; will the government buy the wrong testimony; or will the government make measured and thoughtful use of this dangerous and unseemly but powerful tool? ■

ENDNOTES

1 ©Robert M. Sanger.
2 Title 18 U.S.C. §§ 6001-6005.
3 The district court judge assigned to handle any legal issues arising out of the grand jury.
4 See, e.g., *Kastigar v. United States,* 406 U.S. 441, 453, (1973) and its application in the Oliver North case, *United States v. North,* 920 F.2d 940 (1990).

Robert Sanger is a Certified Criminal Law Specialist and has been practicing as a criminal defense lawyer in Santa Barbara for over 40 years. He is a partner in the firm of Sanger Swysen & Dunkle. Mr. Sanger is Past President of California Attorneys for Criminal Justice (CACJ), the statewide criminal defense lawyers' organization. He is a Director of Death Penalty Focus and a Member of the American Association for the Advancement of Science (AAAS). Mr. Sanger is also a Member of the Jurisprudence Section of the American Academy of Forensic Sciences (AAFS) and Professor of Law and Forensic Science at the Santa Barbara and Ventura Colleges of Law.

Using the Option Pricing Method Changes the Standard of Value: Does the IRS, or Anyone, Care?

By James A. Lisi

Part one of this article presented the 'current method' and 'option pricing method' (OPM) for allocating value to common stock for 409a valuations, and how these two methods differ in pricing of common stock. Part two examines the implied changes made by OPM and how it affects stakeholders. We start with a brief review of the key impacts on the valuation problem.

OPM Impacts on The Valuation Problem

As discussed in part one, OPM implicitly changes the valuation problem. The conflicts between OPM and current value allocation are:

Change in Valuation Subject

OPM shifts the subject of valuation to partial equity interests, versus the company as a whole.

Shift in Valuation Date

Applying probabilities based upon a future exit event moves the valuation date to an arbitrary future date from the present.

Market

Another alteration is replacement of the hypothetical FMV prudent investor with a faceless market.

Common Sense

The pattern of purchase by angel investors and venture capital companies points to a reduction in value for common stock, and a premium for the preferred interests. OPM often has the opposite effect.

James A. Lisi

Accounting Practice

Attempting to compare future values with present values violates accrual accounting principles because future value cannot be earned at the date of valuation.

Once we shift from the control interest to a partial interest, we must also deal with other features of equity blocks. So another important consideration is the type II error - what is missing from OPM.

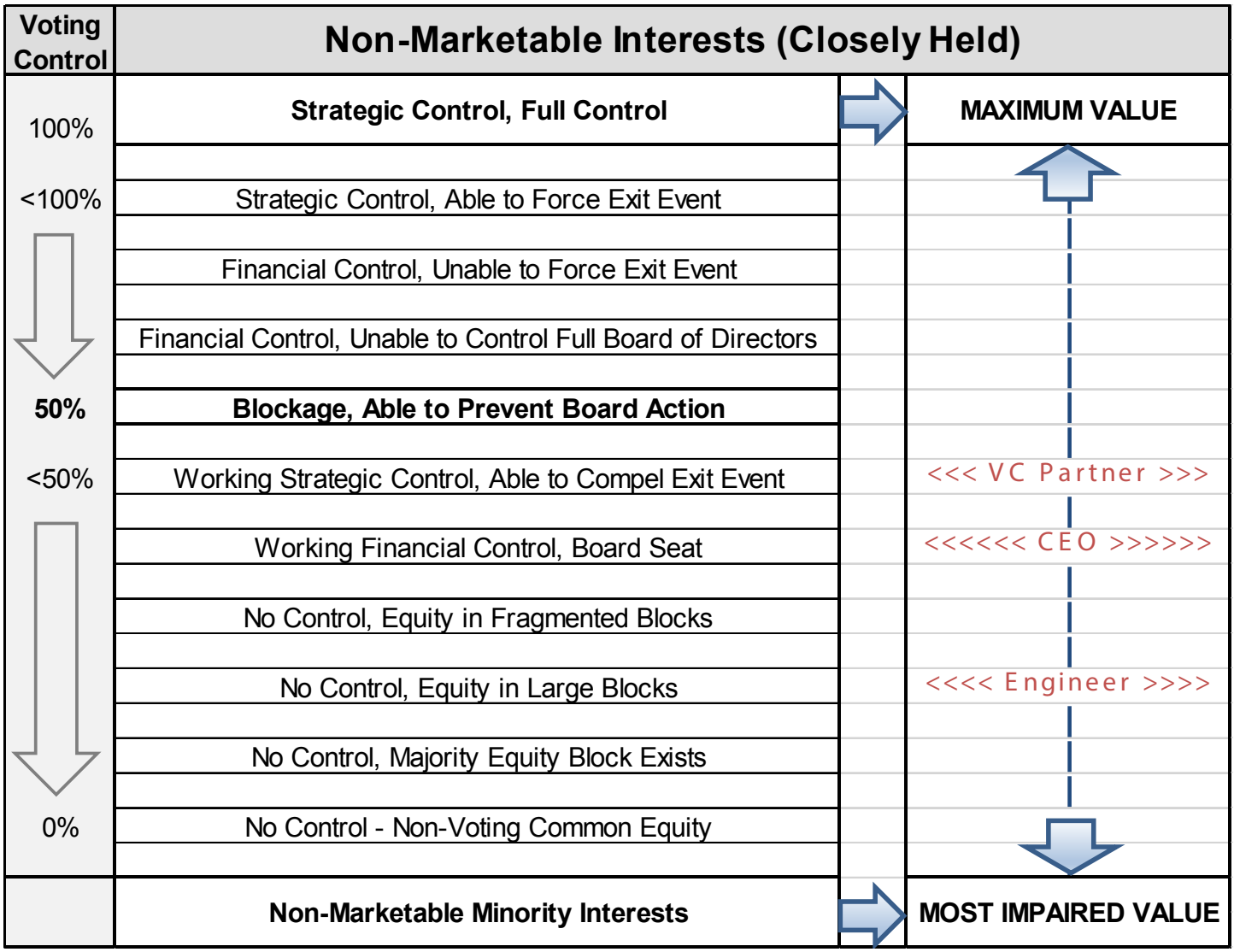
Minority Interests & FMV

We see that OPM makes relative shifts in the allocation of equity between blocks. Valuing equity blocks increases valuation complexity in a quantum jump because we enter into the arena of Discounts for Lack of Marketability (DLOM) to meet the FMV standard of value. To determine relative values between classes, a post OPM DLOM analysis would compare the remaining features and cash flows associated with each equity block to one another. It's a Pandora's box that we do not want to open.

On top of equity characteristics, once the seal has been

broken on judging value between classes, the entire cap table of individual stockholders is drawn into the analysis. DLOM compels us to analyze control influence by the grantee on each issuance. For example, stock option grants to the CEO would have a different strike price than those granted to an engineer, because the CEO has operational control of the company.

For those unfamiliar with the factors involved in establishing a DLOM, the following two charts are presented. The first chart identifies control levels typically used in a DLOM analysis and where the interests would fall for degree of control.



Classifieds

• Price, Postel & Parma LLP, a long-established Santa Barbara law firm, seeks a litigation associate with superior credentials from a major law school, 2-5 years complex litigation experience and a current license to practice in the State of California. Qualified applicants should submit their resume and writing sample to Craig A. Parton via email to the following address: cparton@ppplaw.com.

• Two professional offices available for sublease. Month to month. Has kitchen, bathrooms, parking. $1000/mo. Upper State Street. Call Maureen Clark for details. (805)965-0043.

Value Impairment for Control

And then we would also need to deal with other features of different equity securities and compare them on marketability factors. These factors look like this.

Factor	Impact	Most Impaired Value → Maximum Value
Dollar Size of Interest	Smaller is Better	
Number Qualified Buyers	Higher is Better	
Seller Strategic Position	Stronger is Better	
Information Quality	Higher is Better	
Marketing Time	Lower is Better	
Access to Capital & Financing	Higher is Better	
Cost of Capital & Financing	Lower is Better	
Entry Cost	Lower is Better	
Exit Cost	Lower is Better	
Entry Barriers	Higher is Better	
Exit Barriers	Lower is Better	
Risk	Lower is Better	
Reward	Higher is Better	
Current Annual Return	Higher is Better	
Time to Exit (Return of Principal)	Lower is Better	

Value Impairment for Security Features

A comprehensive analysis of partial interests would require applying all factors relevant to the problem, not only the potential for a distribution from an exit event. Only with a strap-on DLOM comparative analysis can an OPM be justifiably incorporated into the valuation. Otherwise, it is a biased, one-dimensional misapplication of technique.

Regulatory Issues

Based on the above arguments, OPM meets neither the Fair Value (undiscounted) or FMV (discounted) standard of value called out in tax related government regulations, and many company agreements. The analysis is incomplete, so it becomes its own unique value standard.

Being non-compliant with FMV is a vulnerability. It opens the door to all kinds of challenges. The non-compliance issue may be used by an attorney to have a company's historical valuations thrown out as evidence in a dispute. The company would then have no basis to present its value to the court, and the opposing expert's reports would control the question.

An issue also arises around formula approaches, as the Tax Court does not find them to be reliable. IRS Revenue Ruling 68-609 states that the formula method "should not be used if there is better evidence available from which the value of intangibles can be determined." In this regard, the trustworthiness of OPM output is low. The M-B-S formula is highly sensitive to volatility and time to exit, so small changes in these inputs create a wide variation of results. OPM is not only a weak scheme, highly sensitive formulas in general do not produce accurate outcomes. Considering that true volatility of the company's equity is zero, and the time to exit is likely to be a hopeful guesstimate, identifying values to enter into the formula is problematic. If used, some kind of responsiveness test should be added. Sensitivity analysis is demanded for ESOP valuations. Why not 409a valuations?

On the legal front, treasury regulations appear to preclude substituting a public market security as a proxy for the subject being valued. Per IRS Revenue Bulletin 2007-19, section 3b, "The Treasury Department and the IRS believe that the stock right exception under section 409a was intended to cover stock rights *directly reflecting the enterprise value of the entity* for which the service provider is providing services." (Italics added). OPM appears to be an indirect methodology using

proxies for the actual subject.

And our professional standards get in the way. NACVA requires its practitioners to obtain sufficient relevant data on which to base their conclusion. Using only one factor, market volatility, to adjust equity block values, is an incomplete analysis. Evidence exists that other factors, such as control and marketability features, need to be considered. This professional standard is especially worrisome for those valuations using only a previous financing as their sole starting point for determining current value.

Effects of OPM

OK. It is a popular method. So what is the effect of shifting to valuing shares based on future exit value probabilities? Answer: A false sense of security. Mispricing. Poor alignment of performance goals with actual value. Deceiving the workforce.

Setting the strike price of an option at a premium is not an IRS problem. The compliance risk comes when common stock suffers a reduction in value. That is a cause for concern if common stock value falls below FMV and triggers a taxable event.

Practically, however, OPM has significant room in which to err under 409a compliance, because IRS regulations just ask us to define if a taxable income event has occurred. As long as the strike price of the option grant is above the minimum at the time the board approves it, no income tax is incurred.

Setting Strike Price

The minimum value for the strike price is FMV, which includes a discount for Lack of Marketability (DLOM) for non-marketable, non-control interests. However, since we typically want to avoid dilution of existing shareholders, we normally issue new options at Fair Value, the undiscounted value. This practice is documented in accounting directive ASC 718. Fair Value allows us a 20%-50% margin for error.

Setting option strike prices at Fair Value is the best practice. It is equitable to the company, existing shareholders and grantee. It not only deters shareholder suits over unfair dilution, it ensures that the option program provides market rate capital infusions to the company over the long run. Because when the options are redeemed, the option premium is paid to the company, adding to its cash position.

Who cares if we use OPM?

The IRS is looking for untaxed income, so it is doubtful that they will challenge OPM when its use is not expected to reduce value of common stock below FMV. Using OPM for option strike prices has risks, but assuming that the starting current value is soundly developed, the typical unused 20%-50% DLOM would keep most cases above FMV.

As the weakest link in the chain, though, OPM can be attacked for FMV compliance in order to get an entire valuation thrown out. All that needs to be established is that the value conclusion does not meet FMV standards. Then the company is left with no evidence to support its valuation in court.

Executives and other employees may take an interest in the unique 'OPM standard of value' if they feel that the strike price is being unfairly inflated or depressed. The effect is important at the time a grantee receives their options, but also when other grantees get awards afterward. When exits go bad, this is one area where litigation ensues over valuation.

The ones most at risk are CEOs, who are generally the largest benefactors of option grants. If the share price is set in error, they are either accused of unjustly enriching themselves at the expense of other shareholders, or they are cheated out of gains they have rightly earned.

But the true tragedy of OPM happens when non-executive employees commit their careers to a venture, exchanging salary for equity. With companies remaining private longer today, these commitments may now span a decade of service. As their stock grants are given increasing strike prices, purported to be FMV, the key employees believe that they are building wealth. They may even buy stock at these values. Then, the long-awaited exit comes, and these employees find their stock options out of the money because the common stock price is inflated no longer. When the exit occurs, equity blocks can no longer be manipulated by applying mythical volatility, and the current value is at hand. Executives and directors should know better, but engineers, scientists and sales professionals investing their best money-making years in the company are victims of a charade.

Back to Current Value

If we avoid OPM, we never open Pandora's box of having to value equity based on the grantee, nor do we place the CEO and board of directors in jeopardy. Fairness is more assured. The valuation baseline is consistent with any exit. All the complexities of valuing partial interests resolve if we simply use the current value of company equity, and traditional waterfall analysis. No balancing act needs to be executed. All the precepts of accrual accounting and FMV are satisfied as we match all earned value and efforts into

Continued on page 31

Bedsworth, *continued from page 19*

practicing in. Me and Jane Austen.

But wait 'til you see the response to this motion. I can't reproduce the whole thing here. My editors won't approve my check if I just re-type other people's work.[4] The following excerpt should capture its flavor:

So defense counsel Nick Subashi files an affirmative defense criticizing my pleading for having verbose exaggerations and using run-on sentences and "stream of consciousness" rhetoric and what I'd like to know is who does he think he is simply because he represents a major insurance company and can do anything he wants well I'll tell you I don't feel the same way and I think my pleading was perfectly fine after all all I'm doing is representing my clients who have a gigantic 8-figure claim no exaggeration and also particularly since I have extensively researched the defense in this case . . . [25 lines and two citations omitted, but no periods or commas] . . . he probably thinks he is really cool because he practically lives in the gym and he's into rock-climbing and mountaineering like he's the next Reinhold Messner making the first unaided ascent of Everest without supplemental oxygen and gets to go on these adventure trips out west when I'm stuck in the office responding to a defendant's third set of discovery requests and attending multi-hour depositions of witnesses . . . [more omitted here, but no commas or periods] . . . but in any event I hope the judge does not allow Defendant to prevail on this affirmative defense which is as worthless as his other defenses and they should just pay the dough because I just would never resort to stream of consciousness or use run-on sentences or otherwise be verbose but I suppose that's why we have judges who have to make tough decisions and I feel sorry for the Judge anyway because he is a Browns' fan and suffers like everyone else who has the misfortune to follow that inept team for decades and decades and things never improve but speaking of losers did you see that Ohio State offense, and no matter how bad things get it can't be that bad but they were probably overrated anyway and after all spring training is around the corner but the main thing is that I hope the court understands that I would never be verbose or use run-on sentences or put stream of consciousness into a pleading particularly since I have practiced over 38 years and my consciousness is getting pretty impaired and no one pays attention to what I say anyway . . . [ellipsis in original; still no period] Signed, Timothy S. Chappars[5]

To which I say, "Kudos!" Tim Chappars and Nick Subashi are hereby inducted into my own personal litigation Hall of Fame.

Subashi says after years of doing battle, he has the highest respect for Chappars. He calls Chappars' response funny and witty and says, "We lawyers tend to take ourselves way too seriously, so this was a welcome departure from that trend."

It certainly was.

I'm not suggesting you file an answer—or anything more important than a grocery list—that looks like Chappars'. What I'm suggesting is that you strive to practice in such a way that after doing battle with someone for decades, you remain friends, capable of laughing at yourselves. I'm asking you to practice law as a human being rather than a bot.

"And do as adversaries do in law; strive mightily, but eat and drink as friends." That's William Shakespeare. And it's a helluva lot more important than whether you can construct a model sentence.

If you succeed at that, your arteries will remain intact, your garage will grow old and rickety, and your fear of writing will pale into insignificance.

BEDS NOTES

(1) As a second-year law student, working for Continuing Education of the Bar, I suggested edits to Kathryn Werdegar's work. How's that for hubris?

(2) Yeah, I hear you. "Objection, Your Honor. The word 'other' assumes facts not in evidence."

(3) You've come to expect that, right?

(4) Don't you wish?

(5) If you want to see the whole thing (it's worth it just to see the appendix—yes, I said appendix—Chappars attached to his masterpiece), call one of these guys in Xenia or Dayton, or go to Abovethelaw.com, which is a lot funnier than I am anyway. ■

William W. Bedsworth *is an Associate Justice of the California Court of Appeal. He writes this column to get it out of his system. He can be contacted at* ***william.bedsworth@jud.ca.gov****. And look for his new book,* Lawyers, Guns, and Monkeys*, through* ***Amazon*** *and* ***Vandeplas Publishing****.*

Shakespeare's Best Advice, by Justice William W. Bedsworth appeared in the *Orange County Lawyer* March 2017 (Vol. 59, No 3,), p. 71

Motions

Anticouni & Associates is pleased to announce **Tristan Verburgt** has joined the firm as an Associate Attorney. Mr. Verburgt's practice will focus on employment law litigation where he brings extensive jury trial experience. Mr. Verburgt represents both employers and employees in all phases of litigation, including discrimination, harassment, retaliation and wrongful termination cases.

Mr. Verburgt received his Juris Doctorate from the University of San Francisco School of Law, in 2008, where he served as a member of the Environmental Negotiation Team as well as the Investor Justice Clinic.

Prior to joining Anticouni & Associates, Mr. Verburgt was a Deputy District Attorney in Santa Barbara's North County jurisdiction. He managed a caseload of serious and violent felonies, gang cases, domestic violence, white collar and elder abuse cases. During his time as a Deputy District Attorney, he completed multiple felony jury trials for serious and violent felonies including life cases, domestic violence, and sexual assault.

As a Deputy District Attorney, Mr. Verburgt advocated for the victims of serious and violent crimes. He brings his skills and passion to now advocate for the rights of employees and employers.

Jennifer Duffy

Fell, Marking, Abkin, Montgomery, Granet & Raney, LLP is proud to announce that its partner **Jennifer Gillon Duffy** has been named one of the Top 50 Women in Business in the tri-counties for 2017 by the Pacific Coast Business Times. Jennifer is a Santa Barbara native who specializes in employment law and family law. She can be reached at Jduffy@fmam.com and (805) 963-0755.

Congratulations also go out to the other tri-county women attorneys who were chosen for this honor: **Danielle Brinkman (Farber Hass Hurley LLP, Oxnard), Jill Friedman (Myers, Widders, Gibson, Jones & Feingold, Ventura), Karen Gabler (LightGabler, Camarillo), Susan McCarthy (Arnold LaRochelle Mathews VanConas & Zirbel LLP, Oxnard), Leila Noël (Cappello & Noël LLP, Santa Barbara), Robin Paule (Holthouse Carlin and Van Tright LLP, Westlake Village),** and **Amy Steinfeld (Brownstein Hyatt Farber Schreck, Santa Barbara).**

If you have news to report, Santa Barbara Lawyer invites you to "Make a Motion!" Send one to two paragraphs for consideration to our Motions editor, Mike Pasternak at pasterna@gmail.com.

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Instructor: Jeanne Kvale, J.D. and Steve Feder, J.D., (Private practice, Ventura)

10 sessions: up to 26.5 MCLE credits
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For more information or to enroll, please contact Barbara Doyle at Ventura College of Law (805) 765-9302 or email bdoyle@collegesoflaw.edu. Space is limited.
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(MCLE Rules and Regulations, Section 2.80)

Lisi, *continued from page 27*

the same time period.

OPM doesn't reflect reality. It is a solution looking for a problem to solve. It is not worth the risk, the additional cost or destroying the spirit of an entire company when its defects are revealed. ■

James Lisi is a Certified Valuation Analyst located in Santa Barbara, California with over fourteen years valuation experience. His valuations focus on closely-held companies and asset holding entities for tax reporting, while his advisory services support start-up growth companies, transfers and other projects for company owners. He can be reached at james.lisi@americanvaluemetrics.com.

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The SBCBA Real Estate/Land Use Section Presents:

The Impact of SB 1069 and AB 2299 on Residential Accessory Dwelling Units: "Granny Flats" Go Millennial

When:
June 1, 2017, 12:00 p.m.

Where:
Union Bank Community Partners Center
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MCLE:
1.0 Hour (General)

Speaker:
Ariel Calonne, Santa Barbara City Attorney

About the Event:
This presentation will review major 2016 California legislation that significantly expanded the rights of residential property owners to develop accessory (second) dwelling units. The presentation will review the decades of California legislative history in order to place the new legislation into an understandable framework.

Price:
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safety/sheriff-bill-brown-on-law-enforcement-and-immigration/302895351
2 Scott Hennessee, *supra*.
3 8 CFR Section 287.7
4 *Harvey v. City of New York*, No. 07-0343 (E.D.N.Y. June 12, 2009).
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Hornick, *continued from page 10*

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9. *Doctor's Associates, Inc. v. Casarotto* (1996)116 S.Ct. 1652, 1653
10. *Daniels v. Sunrise Senior Living, Inc.* (2013) 212 Cal.App.4th 674, 680

McCready, *continued from page 16*

any kind of a paycheck. They finally borrow money from a relative so that we can help them and we are successful, but when they receive their back pay that they should have received all along, it is without interest or any kind of penalties. Also, they do not receive attorney's fees back when they win. While the system is flawed and the workers' are at a disadvantage, we are here to help them fight for what they deserve. These are people who got hurt doing their job. They should be compensated while they heal and for any permanent injury they suffer. These cases are often easily fixed with the help of an attorney and a doctor, but the claims examiner denies them and most people cannot fight them alone. ■

Michael McCready is the managing attorney of McCready, Garcia & Leet in Chicago. His firm represents injured federal workers in all fifty states and abroad. He can be reached at Info@FederalCompensation.com

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