#N-202 September 14, 1993

Second Supplement to Memorandum 93-31

Subject: Study N-202 — Judicial Review of Agency Action — Scope of Review (Further Comments on Substantial Evidence v. Independent Judgment)

Attached to this memorandum as an Exhibit are additional comments we have received addressed to the issue whether judicial review of administrative factfinding should be on a substantial evidence standard or an independent judgment standard.

Exhibit p. 1 contains language suggested by Professor Asimow helping to elaborate the meaning of the substantial evidence standard and discussing the problem of mixed questions of law and fact in applying the appropriate judicial review standard.

Exhibit pp. 2-6 is a letter from Frederic D. Woocher of Strumwasser & Woocher arguing against the independent judgment standard.

Exhibit pp. 7-8 is a letter from William C. Heath of the California School Employees Association arguing for the independent judgment standard in cases where a fundamental right is involved.

Respectfully submitted,

Nathaniel Sterling
Executive Secretary

DRAFT LANGUAGE FOR COMMENT TO §652.560

1. Before the quotation mark in line 4 of p. 10, add the following sentence: "The substantial evidence standard is not intended to be a judicial rubber stamp; under that standard, the court must conduct a careful and critical scrutiny of the evidence before concluding that the agency's findings are supported by substantial evidence.

2. Delete second ¶ of comment on p. 6 and first ¶ of Staff Note on p. 7.

Add to the comment:

Sections 652.550 and .560 do not resolve the difficult question of whether an issue of application of law to fact (often referred to as a mixed question of law and fact) should be treated for purposes of judicial review as an issue of law or an issue of fact. See Asimow, "The Scope of Judicial Review of Administrative Action" p. 30-32. This issue recurs throughout the law of civil procedure and cannot be resolved for administrative law alone. Therefore, a court must use existing California law in deciding how to classify the application issue; once it is classified, the court should use the appropriate standard as set forth in sections 652.550 and .560.

Existing law treats application questions as questions of fact, rather than questions of law, where the facts of the case (or inferences to be drawn from the facts) are disputed. However, if the facts and inferences are undisputed, the issue is treated as one of law. See Borello & Sons v. Dep't of Industrial Relations, 48 Cal.3d 34, 349, 256 Cal.Rptr. 543 (1989) (whether "sharefarmers" are "employees" treated as question of fact since dependent on resolution of disputed evidence). Perhaps a better test was articulated in Crocker Ntl. Bank v. City of San Francisco, 49 Cal.3d 881, 888, 264 Cal.Rptr. 139 (1989) which decided that whether an item is a "fixture" for tax purposes is a question of law. The Court said: "If the pertinent inquiry [in answering a mixed question] requires application of experience with human affairs, the question is predominantly factual and its determination is reviewed under the substantial-evidence test. If, by contrast the inquiry requires a critical consideration, in a factual context, of legal principles and their underlying values, the question is predominantly legal and its determination is reviewed independently."

file: mixed.draft

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BY FACSIMILE

July 22, 1993

Nat Sterling, Director
California Law Revision Commission
4000 Middlefield Rd., Ste. D-2
Palo Alto, CA 94303-4739

Re: Staff Proposal on Abolishing "Independent Judgment Test" for Judicial Review under the California APA

Dear Mr. Sterling:

We understand that the Commission has before it for consideration a staff proposal to replace the "independent judgment" standard with the "substantial evidence" test for judicial review under the California APA. We are writing to urge the Commission's endorsement of the staff proposal.

Our law firm has developed a practice specialty in the area of administrative law, representing both public agencies and those challenging the administrative actions of various governmental agencies. The lawyers in our firm collectively have devoted almost 50 years of practice to this area, the majority of which has been in the representation of state agencies. A significant portion of our practice over the past three years, in particular, has involved the representation of state Insurance Commissioner John Garamendi in connection with administrative and judicial litigation over the implementation of Proposition 103, the 1988 insurance reform initiative. (I would emphasize, however, that the views expressed in this letter are solely those of our firm, and that we do not here speak for the Commissioner.)

From our experience in this area of the law, we have had a significant opportunity to observe the detrimental consequences of the "independent judgment" standard for judicial review on both administrative agencies and the judiciary. We believe strongly that replacement of the "independent judgment" standard with the "substantial evidence" test is a necessary and sensible development in the law.

As you are undoubtedly aware, the "independent judgment" test is a vestige from an era long since passed, one in which administrative agencies were untested and untrusted, and in which the economic substantive "due process" rights of regulated entities and individuals were deemed paramount to the government's right to protect the public health, safety and

welfare through its regulatory authority. Continued application of the "independent judgment" test in the modern era appears to be unique to California, other jurisdictions having long since abandoned its use in favor of the more deferential "substantial evidence" and "abuse of discretion" standards.

Aside from its now-immaterial historical underpinnings, application of the "independent judgment" test has had considerable adverse impacts in practice. The most direct and deleterious effects, of course, have been on those agencies whose decisions are made subject to independent review in the superior courts. Their decisions and judgments are deprived of the deference which they are due, to be replaced by the independent determinations of a superior court judge who has neither the specific technical expertise nor the broader policy and equitable perspectives that often imbue agency decisions. Moreover, the knowledge that the record developed in the administrative proceedings will be subsequently reviewed in the judicial forum invites the litigants to enlarge the scope of the hearing so as to include each and every issue (however well-established in the administrative arena) that could possibly attract the attention of a superior court judge on review; because of the imbalance of resources typically available to the parties, such an enlargement of the proceedings strains the already limited resources of the agency and can interfere substantially with their ability to serve the public interest.

Beyond the impact on the agencies themselves, however, the "independent judgment" test imposes unwarranted burdens on the judicial system, as well. Because judicial review under that standard is essentially de novo, it effectively gives a dissatisfied litigant a second, "free" bite at the apple. This, of course, creates an incentive for seeking judicial review, adding to the crowded court calendars. For the conscientious superior court judge, moreover, the "independent judgment" test creates an imposing burden, requiring detailed "independent" review of the entirety of an often-voluminous administrative record -- a record that may involve some very complex, technical issues. And the variety of administrative matters that require review preclude the court from developing the kind of expertise that one would hope for, even if the court had the time required to devote itself to this task.

Finally, the "independent judgment" standard does a disservice to the public and to the regulated entities. Forum shopping is invited, inconsistent rulings are promoted, and legislative standards -- rather than being applied consistently by a single agency across different cases and as to different litigants -- are enforced in a haphazard fashion by the thousands

of superior court judges throughout the state. Inequitable treatment is bound to result, and the broader public interest may be sacrificed to the unique views of a single superior court judge.

Our firm's experience in the ongoing litigation over the Insurance Commissioner's implementation of Proposition 103 may provide a concrete illustration of some of the points summarized above. Insurance Code section 1861.09 calls for "independent judgment" judicial review of the company-specific determinations made by the Commissioner in calculating an insurer's rollback obligation under the initiative; the industry-wide regulations adopted by the Commissioner are reviewed under the traditional "substantial evidence" and "abuse of discretion" standards (although the insurers have argued -- thus far unsuccessfully -- for "independent judgment" review of those regulatory standards, as well). In the case of the first insurer called to a company-specific hearing to determine its rollback obligation, dozens of witnesses testified over a 14-day period, approximately 200 exhibits were received in evidence, and an administrative record of over 8,000 pages was compiled. The Administrative Law Judge issued a 200-page proposed decision with detailed findings of fact, which was adopted without modification by the Commissioner. The insurer, 20th Century Insurance Company, filed for review with the Superior Court.

In this specific case, the appeal was heard by a superior court judge who had previously been assigned by the Judicial Council to preside over all Proposition 103-related lawsuits, so she had become familiar with these issues over the past two years of hearing such cases and had been able to adjust her non-Proposition 103 judicial calendar in accordance with the workload demands of those cases. (In the ordinary situation, of course, the insurer's appeal from the agency's decision could be heard by any of thousands of superior court judges throughout the state, and one would not expect the insurer to be unaware of the impact that its choice of forum might have on the outcome of its appeal.) 20th Century's petition for writ of mandate was filed on May 27, 1992. Despite the parties' agreement on the need for expedited consideration, oral argument before the Superior Court did not occur until six months' later, when the court heard approximately 10 hours of argument over a two-day period. Three months after that, the Superior Court issued its 85-page decision, and a final judgment was not entered until March 22, 1993 -- almost 11 months following the Commissioner's decision.

The issues before the Superior Court were extremely complex and technical, centering on some of the most arcane details of economic regulation and insurance accounting:

application of a Capital Assets Pricing Model ("CAPM") to select an authorized rate of return; choosing between direct versus net ratemaking on a written-paid or earned-incurred basis, with the capital base measured by Generally Accepted Accounting Principles (GAAP) or Statutory Accounting Principles (SAP); calculation of the insurer's "minimum permissible earned premium" in accordance with a mathematical ratemaking formula that combines incurred losses, allocated loss adjustment expenses, fixed expenses (capped by an efficiency standard by line of insurance), and ancillary income in the numerator, and a variable expense factor, profit factor, and investment income factor in the denominator, the last factor of which in turn requires calculating the insurer's investment yield on its unearned premium, loss, and loss adjustment expense reserves ratio and on its surplus ratio (which is the reciprocal of its leverage ratio of allowable surplus to written premium). I am sure you understand the point: The Superior Court was called upon to "independently review" and analyze thousands of pages of an administrative record dealing with complex issues that only an experienced insurance actuary could learn to appreciate.

Moreover, given the constraints imposed by the judicial process, the court was left to analyze these issues with only limited opportunity for give-and-take with counsel or colleagues. Conversely, counsel were forced to brief and present their cases with no ability to anticipate which of the myriad technical issues might cause the court confusion, which needed particular clarification and emphasis. Indeed, it was not until the court issued its ruling that the litigants could know whether the court understood even the most fundamental premises underlying the agency's decision, premises so basic that those already familiar with them paid them little heed in the administrative process only to discover that the concepts were not understood by a superior court judge who was not as expert in standard insurance accounting and economic matters.

As this example illustrates, the simple fact is that most administrative determinations are ill-suited to de novo review in the superior courts: Administrative agencies can be thwarted in fulfilling their mandates, courts are unfairly burdened with the task of reviewing highly technical issues, and litigants may be subject to unwittingly misinformed judicial decisions.

If there is a concern regarding potential regulatory overreaching, it is best addressed by enforcing the existing requirements regarding the development of a complete record for judicial review, the adequacy and specificity of findings, and the clarity of the agency's statement of the basis for its

decision. Neither the private interests of the regulated entities nor the broader public interests are well-served by permitting the superior court simply to substitute its judgment for that of the expert agency. We urge you to adopt the staff's recommendation to inter the "independent judgment" test and replace it with the "substantial evidence" standard for judicial review.

Thank you for providing us with the opportunity to share our perspective with the Commission on this important issue. If we can be of any further assistance in the Commission's consideration of this matter, please feel free to call upon us.

Sincerely yours,

Fredric Woocher

Fredric D. Woocher

California School Employees Association

September 10, 1993

Sanford Skaggs, Chairperson
California Law Revision Commission
4000 Middlefield Road, Suite D-2
Palo Alto, California 94303-4739

Re: **Scope of Judicial Review**

Dear Chairperson Skaggs and Members of the Commission:

On September 24, 1993, the Commission will consider the standard for judicial review of agency factfinding. The staff alternatives set forth in the note to Memorandum 93-31, section 652.560, do not include any example whereby the choice between independent judgment/weight of the evidence review and rational basis/substantial evidence review is based on whether a fundamental right is affected. The comment states that such a distinction makes no sense. (Memorandum 93-31, pp. 7-8.) I disagree.

The right of a permanent public employee to continued employment, absent just cause for termination, is fundamental. (Pipkin v. Board of Supervisors (1978) 82 Cal.App.3d 652, 661.) The right of a permanent public employee to assign a particular grade to a student is not fundamental. (Eureka Teachers Association v. Board of Education (1988) 199 Cal.App.3d 353, 366.) The distinction between these two rights in terms of their importance to the employee's life situation is obvious. While there are no bright-line boundaries to "fundamentalness" such distinctions are not "utterly incoherent". (Contra, Memorandum 93-23, p. 24.) Some flexibility of "fundamentalness" is essential in a changing society.

I agree that it makes no sense to distinguish factfinding in constitutional and nonconstitutional agencies. (See Memorandum 93-31, comment, p. 7.) However, the recommendation to dispense with the independent judgment test resolves the inconsistency by moving in the wrong direction. The importance of the right affected should determine the intensity of judicial review.

Professor Asimow's recommendation depends upon Tex-Cal Land Management, Inc. v. Agricultural Labor Relations Board (1979) 24 Cal.3d 335, where the Court declined to invalidate a deliberate legislative choice of the substantial evidence test. Significantly, the Court's holding included the specific safeguards required by the Agricultural Labor Relations Act (ALRA).

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> "We therefore hold that the Legislature may accord finality to the findings of the statewide agency that are supported by substantial evidence on the record considered as a whole and are made under safeguards equivalent to those provided by the ALRA for unfair practice proceedings, whether or not the California Constitution provides for that agency's exercising 'judicial power'." (Id. 24 Cal.3d at 346, emphasis added.)

As the Court noted, the ALRA mandates many procedural safeguards, including the separation of prosecutorial from adjudicatory functions (Labor Code § 1149), notice, written pleadings, evidentiary hearings (Labor Code § 1160.2), and a requirement that orders be accompanied by findings based on the preponderance of the reported evidence (Labor Code § 1160.3). Since the proposed new APA does not mandate such safeguards for all agencies, or even for all state agencies, it does not follow from Tex-Cal that the Legislature can mandate substantial evidence review for all agency adjudications.

The proposed new APA mandates these safeguards only for hearings required to be conducted by an administrative law judge employed by the Office of Administrative Hearings (OAH). In light of Tex-Cal, the Legislature could mandate substantial evidence review of factfinding in such hearings, provided the agency did not change the findings of the OAH administrative law judge. Under both the State Constitution and public policy, the independent judgment test must apply to all other cases where a fundamental right is at stake.

Thank you for the opportunity to present these comments to the Commission.

Sincerely,

William C. Heath

WILLIAM C. HEATH
Deputy Chief Counsel

WCH:ws

cc: Bud Dougherty, ED
Margie Valdez, CC
Barbara Howard, DGR