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Don DeBenedictis / Daily Journal

David J. Pasternak, receivership lawyer and former head of organizations including the L.A. County Bar Association, Bet Tzedek, and the Chancery Club, was voted in Friday by the bar board of trustees to be the next president of the California State Bar. Among his priorities, Pasternak has vowed to improve access to justice and increase court funding.

GUEST COLUMN

Dewey learn anything?

By Edwin B. Reeser

The take away from the criminal case against former managers of Dewey & LeBoeuf LLP — the once global, now failed mega law firm — is not the immediate listing of all the ways that "we [i.e., your firm] are different." It is the more deliberate embrace of a careful examination of how we are the same.

Dewey did not collapse because its leaders were corrupt, or mean spirited, or greedy, or incompetent. Those elements, if present, wouldn't help, but if absent wouldn't save the firm either. Dewey's collapse was a simple demonstration that firms don't die for lack of profit, but for lack of *cash*.

It was the cash flow paradigm — distributing more dough to partners than the firm earned — that did Dewey in. When the cash flow requirements for making distributions could not be sustained from operations, the money was borrowed, literally from every point on the compass.

It was borrowed on the working line of credit from banks.

It was borrowed in the capital markets with a private bond offering.

It was "borrowed" from partners with a large capital contribution requirement enabled with a unique "100 percent financing with interest paid by the firm" personal recourse loan to partners.

It was "borrowed" from retired partners by reducing their distributions.

It was "borrowed" from withdrawn partners by withholding and amortizing the return of their capital accounts over a term of years.

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DAILY APPELLATE REPORT

CIVIL LAW

Civil Procedure: In first impression review, court justified in re-empanelling jury 'moments' after dismissal to correct verdict error as inquiry satisfies issue of outside influence. *Dietz v. Bouldin,* USCA 9th, DAR p. 8486

CRIMINAL LAW

Criminal Law and Procedure: In lead case, Proposition 47's offense reclassification provisions under Penal Code Section 1170.18 applies to juvenile offenders, authorizing redesignation of juvenile felony to misdemeanor. *Alejandro N. v. Superior Court (the People),* C.A. 4th/1, DAR p. 8475

Criminal Law and Procedure: Trial court errs in imposing period of parole in resentencing offender under Prop. 47, without accounting for custody credits and where resulting period exceeded remainder of his post-release community supervision. *People v. Pinon,* C.A. 4th/3, DAR p. 8482

Trustees vote to cut length of bar exam

By Don J. DeBenedictis
Daily Journal Staff Writer

LOS ANGELES — California's difficult, exhausting bar exam will shrink from three full days to two days beginning in July 2017, State Bar trustees decided Friday.

Voting unanimously after only limited debate, the bar board adopted a proposal to alter the format of the exam — largely unchanged for more than 25 years — with the goal of improving efficiency and saving $1 million a year.

Future exams will have only five one-hour essay questions, instead of six, and only one 90-minute performance test essay rather than two 3-hour performance tests. The daylong multiple-choice portion of the test, the national Multistate Bar Exam, will remain as is.

The change will bring California in line with most other U.S. jurisdictions. Only two other states, Louisiana and South Carolina, give three-day exams. Several give 2½-day exams. Sixteen states use a national two-day test called the Uniform Bar Exam prepared by the National Conference of Bar Examiners, the organization that creates the national multiple choice test.

The bar's Committee of Bar Examiners has investigated whether and how to trim the exam since 2011, and its final recommendation easily passed a committee of the bar trustees on Thursday.

On Friday, Los Angeles trustee Hernan Vera questioned whether one of the changes might hurt minority or disabled bar applicants. He told the board that he had received an e-mail from Susan Westerberg Prager, dean of Southwestern Law

See Page 3 — TRUSTEES

State Bar elects a new president

By Don J. DeBenedictis
Daily Journal Staff Writer

LOS ANGELES — Promising to improve efficiency and transparency, David J. Pasternak, a receivership lawyer and longtime bar activist, was elected Friday to be the next president of the State Bar.

The bar board of trustees voted 9 to 7 for Pasternak over Heather Linn Rosing of San Diego, the bar's current vice president.

In a presentation to the trustees before the voting, Pasternak said his priorities also include improving access to justice for the poor and increasing funding for the courts. Public protection is the State Bar's main mission, he said, but that must include keeping courts open. "If the public doesn't have access to the courts, how can it be protected?" he asked.

A former president of the Los Angeles County Bar Association, Pasternak, 64, has also headed Bet Tzedek Legal Services, the Chancery Club and an advisory committee to the Los Angeles City Council. He is also the first trustee appointed to the bar board by the state Supreme Court.

In a written campaign statement, he noted that he has "extensive experience with processes of transition and changed leadership" for troubled businesses based on his 25 years of practice as a court-appointed receiver or receiver's attorney. That experience will be important in the coming year, he said.

The State Bar is slowly recovering from the controversy and ongoing litigation over its November termination of former state Sen. Joseph L. Dunn as its executive director. *Dunn v. State Bar,* BC563715 (L.A. Super. Ct., filed Nov. 13, 2014)

See Page 3 — STATE

After defense verdict, judge orders retrial in tainted Tylenol case

By America Hernandez
Daily Journal Staff Writer

A federal judge has ordered a new trial against pharmaceutical giant Johnson & Johnson after an evidentiary hearing revealed several jurors discussed Internet-obtained research while deliberating on a wrongful death suit involving children's Tylenol. *Robertson et al v. McNeil - PPC Inc. et al*, 2:11cv9050 (C.D. Cal., filed Nov. 1, 2011).

In 2011 Kindra and Peter Robertson filed suit against Johnson & Johnson and the manufacturing plant that produces children's Tylenol after their 11-year-old son passed away from a bacterial infection days after ingesting the medicine, according to court documents.

Batches of children's Tylenol had been pulled from shelves as part of a "phantom recall," where a company purchases all available stock to remove it from the marketplace in lieu of issuing formal recall announcements.

The suit was filed after Johnson & Johnson was called to testify before the U.S. Congressional Committee on Oversight and Government Reform for not having issued press releases in what has since been labeled the largest children's medicine recall in the country, affecting more than 135 million units tainted with bacteria and small metal parts.

The jury delivered a complete defense verdict.

One juror admitted immediately after trial that she found information online about the recall before a verdict was reached, but did not see the particular batch in question listed among those recalled and thus assumed that the death of the plaintiff's child was unrelated. The comment alone was insufficient to request a new trial since it amounted to hearsay, said plaintiff's attorney Browne Greene, name partner at Greene Broillet and Wheeler LLP.

Greene hired professional investigators to reach out to each juror and take depositions to include in posttrial motions, which revealed that several additional jurors, including the foreperson, had also done research and shared outside information.

"The ironic thing about the jurors who did their investigation on the Internet was that they got the wrong information; they found that the recalls did not include the batch our client's bottle was in when in fact it was recalled," Greene said. "They had been voting for the mother but then turned around and voted for the defense."

Defendants Johnson & Johnson and McNeil-PPC Inc. were represented by Su-Lyn Combs and William H. Dance of Tucker Ellis LLP. Calls for comment were not returned.

See Page 3 — JUDGE

One bite of the apple in requests for relief

By Alana Rotter

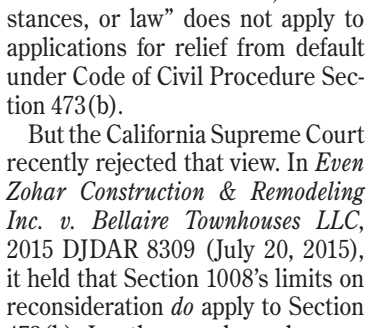
Are attorneys entitled to a do-over if the court denies their first request for relief from a default?

Several Courts of Appeal have suggested that the answer is yes — specifically, that Code of Civil Procedure Section 1008's rule that courts cannot grant a motion for reconsideration unless it is based on "new or different facts, circumstances, or law" does not apply to applications for relief from default under Code of Civil Procedure Section 473(b).

But the California Supreme Court recently rejected that view. In *Even Zohar Construction & Remodeling Inc. v. Bellaire Townhouses LLC*, 2015 DJDAR 8309 (July 20, 2015), it held that Section 1008's limits on reconsideration *do* apply to Section 473(b). In other words, make your first request for relief as compelling as you can, because you are not likely to get a second chance if the court denies it.

Zohar involved a common scenario: The trial court entered a default judgment after defendants failed to respond to a complaint, and the defendants sought relief from the default under Code of Civil Procedure Section 473(b)'s provision that the court "shall" vacate a default judgment "whenever an application for relief is made no more than six months after entry of judgment, is in proper form, and is accompanied by an attorney's sworn affidavit attesting to his or her mistake, inadvertence, surprise, or neglect."

The defendants' Section 473(b) application asserted that their attorney missed responding to the complaint because he had been away from the office on personal matters, and his staff failed to properly maintain the file. But the trial court rejected that explanation as "not credible" and "entirely too general" in light of evidence that plaintiff had repeatedly alerted defense counsel to the impending default, and denied relief.

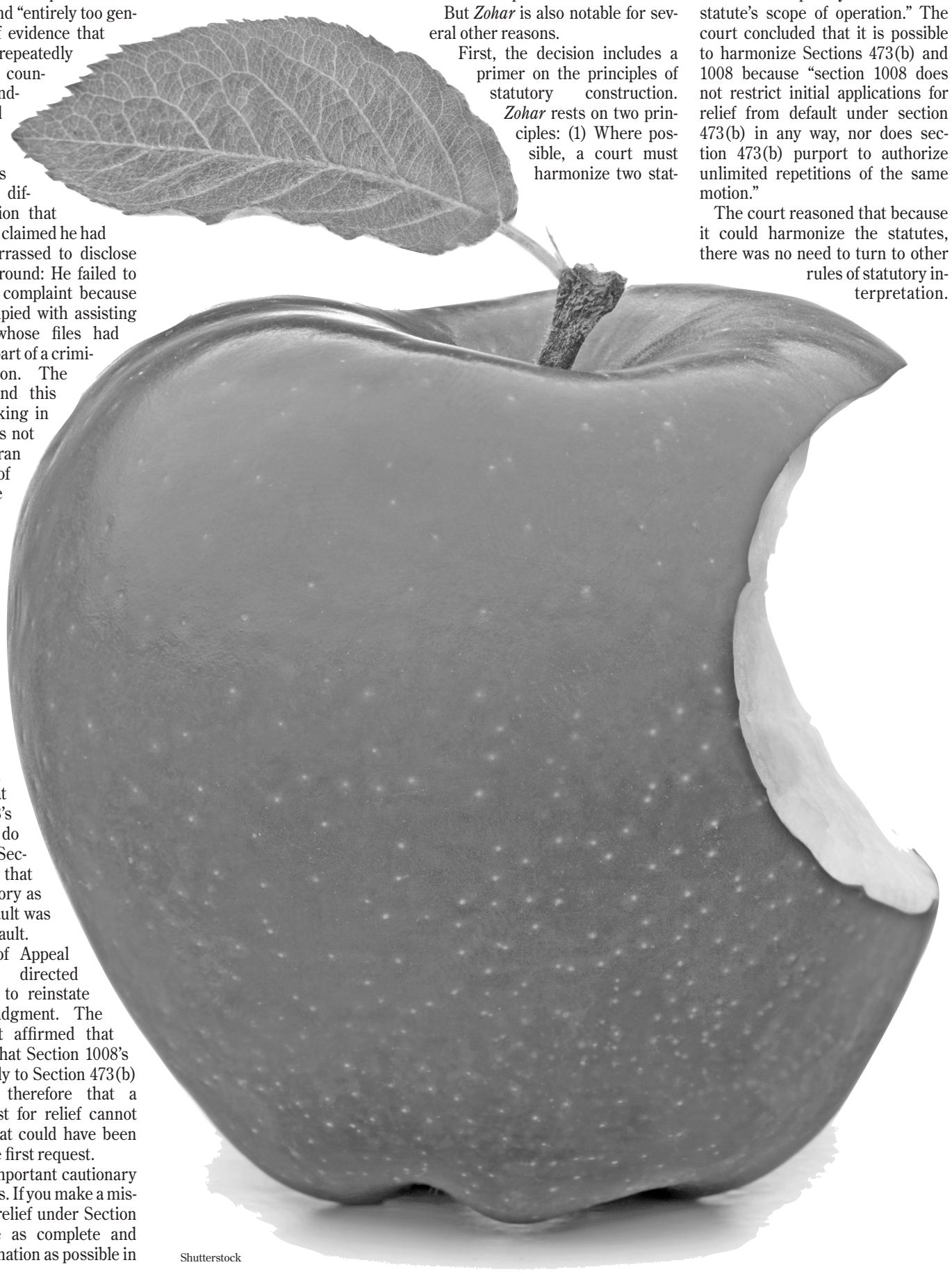


ALANA ROTTER
Greines, Martin Stein & Richland

Defendants tried again, this time offering a different explanation that defense counsel claimed he had been too embarrassed to disclose the first time around: He failed to respond to the complaint because he was preoccupied with assisting other clients whose files had been seized as part of a criminal investigation. The trial court found this explanation lacking in two ways: It was not credible, and it ran afoul of Code of Civil Procedure Section 1008 because it was based on facts that the attorney knew when he filed the prior Section 473(b) application. But the court nonetheless granted relief, based on an appellate decision suggesting that Section 1008's requirements do not apply to Section 473(b) and that relief is mandatory as long as the default was not the client's fault.

The Court of Appeal reversed and directed the trial court to reinstate the default judgment. The Supreme Court affirmed that ruling. It held that Section 1008's restrictions apply to Section 473(b) requests, and therefore that a renewed request for relief cannot rely on facts that could have been presented in the first request.

Zohar is an important cautionary tale for attorneys. If you make a mistake and need relief under Section 473(b), provide as complete and honest an explanation as possible in the accompanying affidavit. If you provide only a partial or misleading explanation and the court denies the motion, it will be too late to fill in the gaps — unless there are new factual or legal developments after the first motion for relief is denied, Section 1008 will compel denying a renewed request for relief.



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But *Zohar* is also notable for several other reasons.

First, the decision includes a primer on the principles of statutory construction. *Zohar* rests on two principles: (1) Where possible, a court must harmonize two statutes, giving full effect to both; and (2) there is a presumption against repeals by implication, "including partial repeals that occur when one statute implicitly limits another statute's scope of operation." The court concluded that it is possible to harmonize Sections 473(b) and 1008 because "section 1008 does not restrict initial applications for relief from default under section 473(b) in any way, nor does section 473(b) purport to authorize unlimited repetitions of the same motion."

The court reasoned that because it could harmonize the statutes, there was no need to turn to other rules of statutory interpretation. Among the rules that the court declined to rely on were that a specific statute trumps a general one, and that a newer statute takes precedence over an older one (unless these two rules point in different directions, in which case specificity trumps timing, see *State Dept. of Public Health v. Superior Court*, 60 Cal. 4th 940, 960 (2015). The court explained that those are merely "tie-breaking rules" to apply where two statutes in fact conflict. If there is a way to give effect to both statutes, a court will do so without looking to the "tie-breaking" considerations.

Second, *Zohar* highlights the difficulty of reading tea leaves when it comes to Supreme Court grants or denials of review. The same issue presented in *Zohar* — the interaction of Sections 473(b) and 1008 — had come up in at least three prior published decisions, in 2002, 2009 and 2010. Each of those three opinions suggested that Section 1008 does not apply to Section 473(b) applications for relief from default. There were petitions for review filed in two of the cases, and the court denied both. Only after the *Zohar* Court of Appeal adopted an opposing view — that Section 1008 limits Section 473(b) applications — did the Supreme Court grant review of the issue. It then affirmed *Zohar*'s position, and disapproved of the three prior cases — including the two in which it had denied review.

The decision to grant review in *Zohar* but not in the earlier cases could reflect many factors, including changes in the composition of the Supreme Court since the issue was last presented. But regardless of the explanation, the point remains: The denial of a petition for review does not necessarily mean that the court agrees with the decision below, and a grant of review does not necessarily indicate that the court is prepared to reverse. Only time — and the Supreme Court's decision on the merits — will tell.

Alana Rotter *has been named a Rising Star in Appellate Law by Super Lawyers each year since 2013 and is a partner at Greines, Martin, Stein & Richland LLP, which focuses on civil appeals and writs. She is certified as an appellate specialist by the State Bar of California Board of Legal Specialization. She can be reached at arotter@gmsr.com.*

Embrace how we [your firm] and Dewey are the same

Continued from page 1

It was "borrowed" from vendors with deferrals of payments.

When that was no longer enough to sate the demand, it was "borrowed" by accounting legerdemain, with a finance department that became the most important "profit center" in the firm.

This went beyond flexibility in accounting treatments, which was probably aggressive to say the least. The trial has focused on the blatantly fraudulent treatments, but it is likely that many "gray area" treatments were exhausted before the firm defaulted to the use of bold lies — treatments such as longer amortization terms for equipment to reduce that expense (thus inflating profits) and capitalizing recruiter and pipeline start-up expenses for lateral hires (thus inflating profits).

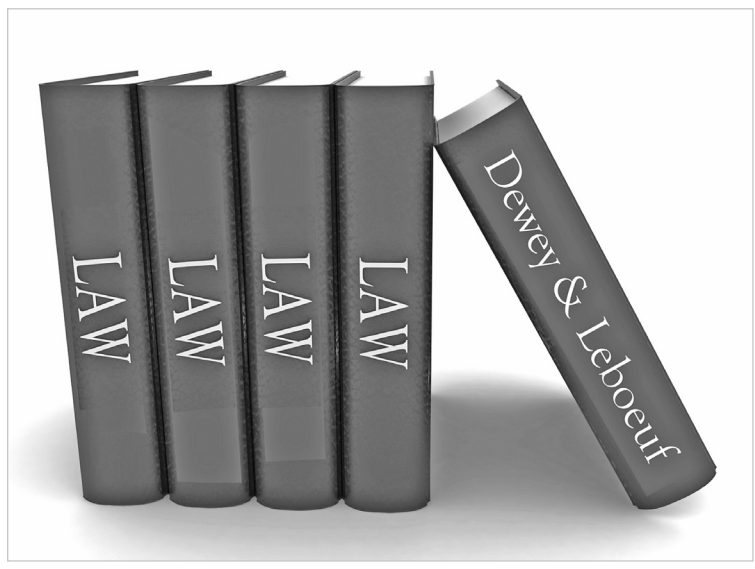
Then the bad stuff: retroactively recharacterizing salary expense to "of counsel" as profits shares (thus inflating profits), back dating checks (thus inflating profits) and recharacterizing expense reimbursements as fees. The list goes on.

All of these work to not only overstate income, in Dewey's case by tens of millions of dollars a year, each year — which adds up to nine figures rather quickly — but to then enable the making of more distributions as coming from profits. But those distributions didn't come from profits; they came from the previously identified "borrowings."

Does it strike anyone as a bad idea to take "after tax money" — which is what equity/debt is — and pay it to yourself as income you then pay more tax on? Taking money from partner capital and bank/bond debt is nothing less than looting the balance sheet — stealing money from future periods through distributions today against what is the collateral for the borrowings — the accounts receivable. And ultimately stealing from oneself, and for perhaps a few persons, stealing from their partners.

This acceleration of distributions relative to actual collections compresses the balance sheet to where partners, current and future, would be working for years to make up the deficit created by those who took the distributions.

Why would anyone choose to stay in a firm and do that? Not the exploited partners, if they realized it. Not the exploiting partners once the game is no longer sustainable without them taking a massive cut in distributions. Everybody will run for the elevators.



The New York Times

The frightening part of this is that while the Dewey dilemma ultimately fell into what was perhaps a criminal enterprise (that remains to be proven), it was absolutely an incredibly ill-considered business model that virtually guarantees failure *even without the presence of fraud*. If there was fraud at Dewey, it just perpetuated the scheme a couple more years and left a bigger crater for the lenders. The partners ultimately didn't wind up paying much of it back as a percentage of the loss or their exposure to clawbacks in the bankruptcy.

Is Dewey alone in this respect? Absolutely not. We know that as far back as 2011 the Wall Street Journal reported that over half of the AmLaw 50 were, according to Citibank, materially misreporting their profits: 11 of them by … wait for it … more than *20 percent*. One of them, it turns out, was Dewey. Is this behavior limited to the AmLaw 50? The AmLaw 100? The NLJ 250? Why would it stop at #51?

Debt versus no debt is irrelevant to the problem. A heavily capitalized firm with equity only and no borrowings is *no less at risk* than one that uses a measure of both, or heavy debt.

Can a firm that has fallen into the trap of over statement of income in an effort to hold on to their partners — to "save the firm," by enabling just that amount of over distribution to keep things glued together until "next year" — be triaged, and then reversed? If you are the new managing partner and inherit something like this (forget for the moment the predecessors who may have been responsible for the "great idea" that implemented or prolonged it), how does one go about fixing the problem, to really save the firm? Or does the past adoption of this easily available "drug" of financial engineering basically mean the demise of the firm?

The overstatement of income in the past to get to where you are now requires the understatement of income and lower distributions in the future to pay the piper back. It is most unlikely that those who benefitted from the over distributions will be burdened with the future under distributions in the same amounts, if at all. A failure to reconcile this means you have to maintain certain accounting conventions that are questionable at best just to stay even with your actual current and future year performances. And as the managing partner, you know and are responsible for doing that.

Ladies and gentlemen, if you are the leader, what would you do? How can you get partner support? If you are a partner, what would you be willing to sacrifice for the firm to get it done? The question is coming to firms near you. If the leadership is not empowered by the partners to make the change, because the partners support it with reduced income reality, it probably can't be done. This is not a hypothetical and it has to be addressed. We [*your* firm] may not be Dewey, but we don't have to be to suffer the same basic outcome.

Edwin B. Reeser *is a business lawyer in Pasadena specializing in structuring, negotiating and documenting complex real estate and business transactions for international and domestic corporations and individuals. He has served on the executive committees and as an office managing partner of firms ranging from 25 to over 800 lawyers in size.*

EDWIN REESER
Pasadena

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