

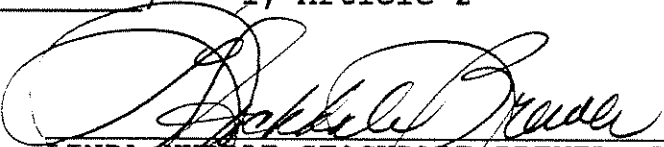
CALIFORNIA OFFICE OF ADMINISTRATIVE LAW  
SACRAMENTO, CALIFORNIA

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MARCH FONG EU  
SECRETARY OF STATE  
CALIFORNIA

In re: )  
Request for Regulatory )  
Determination filed by )  
Michael J. Siegel )  
concerning the Board of )  
Dry Cleaning and Fabric )  
Care's surety bond waiver )  
policy<sup>1</sup> )  
1987 OAL Determination No. 2  
[Docket No. 86-008]  
February 11, 1987  
Determination Pursuant to  
Government Code Section  
11347.5; Title 1, California  
Administrative Code, Chapter  
1, Article 2

Determination by:

  
LINDA HURDLE STOCKDALE BREWER, Director

Herbert F. Bolz, Coordinating Attorney  
Rulemaking and Regulatory  
Determinations Unit

THE ISSUE PRESENTED <sup>2</sup>

Michael J. Siegel has requested the Office of Administrative Law (OAL) to determine whether or not the Board of Dry Cleaning and Fabric Care's (BDCFC) policy of accepting unsecured guaranties in lieu of the surety bonds required by the Business and Professions Code [former section 9747, now 19233] is a regulation as defined in Government Code section 11342(b) and is therefore invalid and unenforceable unless adopted as a regulation and filed with the Secretary of State in accordance with the California Administrative Procedure Act (APA).<sup>3,4</sup>

THE DECISION <sup>5,6,7</sup>

The Office of Administrative Law finds that the above noted policy (1) is subject to the requirements of the APA, (2) is a regulation as defined in the APA, and is therefore invalid and unenforceable unless adopted as a regulation and filed with the Secretary of State in accordance with the APA.

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I. AGENCIES, AUTHORITY, APPLICABILITY OF APA; BACKGROUND

Agencies

In this matter, three noteworthy developments have occurred since the filing of the Request in April 1986. First, the Board of Dry Cleaning and Fabric Care (BDCFC), the agency whose informal rule was originally challenged, has been abolished by the Legislature. However, the pertinent statutory function, requiring dry cleaners to post consumer-protection surety bonds as a condition of licensure, was transferred to another agency within the Department of Consumer Affairs--the Bureau of Home Furnishings (BHF). Second, the re-enacted bond statute was modified effective January 1, 1987, to more specifically authorize the long-established custom of accepting unsecured guaranties in lieu of bonds, provided that the custom was adopted in regulation. Third, legislation was introduced on December 4, 1986 which would waive the bond requirement for some licensees and direct the BHF to accept unsecured guaranties from the remaining licensees.

We also take note of two events which have not occurred: the BHF has neither (1) filed with OAL regulations designed to legalize the unsecured guaranty policy inherited from the BDCFC nor (2) acted on OAL's invitations to formally comment upon these proceedings. We thus have no evidence in the record that the challenged policy has been either validated or abandoned.

Since responsibility for enforcing the statutory bond requirement has been transferred to BHF, we conclude that it is appropriate to complete the AB 1013 review process by issuing a determination.

Authority <sup>8</sup>

Business and Professions Code section 19034 provides in part that:

"With the approval of the director [of Consumer Affairs], the chief [of the Bureau of Home Furnishings] may adopt rules and regulations necessary for the administration of this chapter [chapter 3 of division 8 of the B & P Code] and declaring the policy of the bureau . . . . " [Emphasis added.]

Business and Professions Code section 19233(b) (formerly 9547, paragraph 3) provides:

"If, however, upon application and any proof as the bureau [formerly, BDCFC] may require, the bureau [formerly, BDCFC] determines that the financial

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responsibility of any registrant is acceptable in the public interest, the bureau [formerly, BDCFC] may waive the filing of the security or bond in accordance with any conditions as may be prescribed by the rules and regulations of the bureau [formerly, BDCFC]." [Emphasis added.]

Business and Professions Code section 19233(g), (effective January 1, 1987) provides:

"The bureau may adopt rules and regulations which authorize the bureau to waive the filing of the security or bond if, upon application and any proof as the bureau may require, the bureau determines that the registrant's responsibility is guaranteed by any third party whose financial responsibility is sufficient and acceptable in the public interest." [Emphasis added.]

#### Applicability of the APA to Agency's Quasi-Legislative Enactments

The APA applies by its terms to all state agencies, except those "in the judicial or legislative department."<sup>9</sup> Since BDCFC was not and BHF is not in either the judicial or legislative "department," we conclude that APA rulemaking requirements generally (a) applied to BDCFC and (b) apply to BHF.<sup>10</sup>

Additionally, Business and Professions Code section 19034.5 provides that:

"All rules and regulations [of BHF] shall become effective not earlier than 30 days after approval by the director [of Consumer Affairs], and upon compliance with the procedure provided in [the APA]." [Emphasis added.]

#### Background

The following undisputed facts and circumstances have given rise to the present Determination.

On March 21, 1986, the Deputy Director/Chief of Legal Affairs of the Department of Consumer Affairs advised the Executive Officer of the BDCFC by memorandum that the Board should discontinue its practice of accepting unsecured guaranties in lieu of the surety bond required by law. (Attached as Exhibit A.) In a Board letter dated April 4, 1986, apparently initiated by the Executive Officer, licensees were advised to promptly obtain proper surety bonds or else face automatic suspension of their licenses. (Attached as Exhibit B.) In a second Board letter dated April 10, 1986, signed by the Board President, licensees were advised to "disregard" the bond submission deadlines set out in the April 4 letter and to await development of alternative solutions to the problem. (Attached as Exhibit C.) At an April 21, 1986 public meeting, the Board apparently voted to continue to

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accept unsecured guaranties in lieu of the statutorily-required surety bond.

Responding to the April 21, 1986 decision to continue the waiver policy, Michael J. Siegel (who had served as BDCFC Executive Officer until mid-April) filed a Request for Determination with OAL on April 28, 1986.

II. DISCUSSION OF DISPOSITIVE ISSUES

There are two main issues before us:11

- (1) WHETHER THE CHALLENGED RULE IS A REGULATION WITHIN THE MEANING OF THE KEY PROVISION OF GOVERNMENT CODE SECTION 11342.
- (3) WHETHER THE CHALLENGED RULE FALLS WITHIN ANY ESTABLISHED EXCEPTION TO APA REQUIREMENTS.

FIRST, WE INQUIRE WHETHER THE CHALLENGED RULE IS A "REGULATION" WITHIN THE MEANING OF THE KEY PROVISION OF GOVERNMENT CODE SECTION 11342.

In pertinent part, Government Code section 11342(b) defines "regulation" as:

". . . every rule, regulation, order or standard of general application or the amendment, supplement or revision of any such rule, regulation, order, or standard adopted by any state agency to implement, interpret, or make specific the law enforced or administered by it, or to govern its procedure . . . ." [Emphasis added.]

Government Code section 11347.5, authorizing OAL to determine whether or not agency rules are "regulations," provides in part:

"No state agency shall issue, utilize, enforce or attempt to enforce any guideline, . . . manual, instruction [or] . . . standard of general application which is a regulation as defined in subdivision (b) of section 11342, unless the guideline, . . . manual, instruction [or] . . . standard of application . . . has been adopted as a regulation and filed with the Secretary of State pursuant to this chapter . . . ." [Emphasis added.]

Applying the definition of "regulation" found in Government Code section 11342(b) involves a two-part inquiry.

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First, is the informal rule either

- o a rule or standard of general application or
- o a modification or supplement to such a rule?

Second, does the informal rule either

- o implement, interpret, or make specific the law enforced or administered by the Department or
- o govern the Department's procedure?

The answer to both parts of this inquiry is "yes."

The decision to waive the bond requirement is a modification of or supplement to the bond statute--Business and Professions Code section 19233(b) (formerly 9547, paragraph 3)).<sup>12</sup> The modification applies to all dry cleaners required to be licensed by the Board.

Further, the waiver policy implements the law enforced by the Board (the bond statute).

In June 1985, the Department filed with OAL a proposed amendment to the CAC which effectively conceded that policies supplementing statutory provisions on bonds should be formally adopted as regulations. This 1985 proposal to amend Title 16, CAC, section 516 purported to validate the bond waiver policy. Because of a number of substantive and procedural deficiencies, the amendment was not approved by OAL.

Additional evidence that the waiver policy constitutes an informal modification of the bond statute may be found in the advice memo sent to the BDCFC by the Department of Consumer Affairs.

SECOND, WE INQUIRE WHETHER THE CHALLENGED RULE FALLS WITHIN ANY LEGALLY ESTABLISHED EXCEPTION TO APA REQUIREMENTS.

Rules concerning certain activities of state agencies--for instance, "internal management"--are not subject to the procedural requirements of the APA.<sup>13</sup> We conclude that none of the recognized exceptions (set out in note 13) apply to the bond substitution policy.

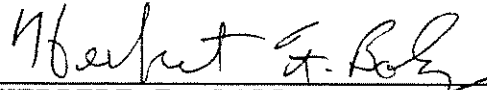
### III. CONCLUSION

For the reasons set forth above, OAL finds that the challenged bond waiver policy (1) is subject to the requirements of the APA, (2) is a regulation as defined in the APA and is therefore invalid and unenforceable unless

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adopted as a regulation and filed with the Secretary of State  
in accordance with the APA.

DATE: February 11, 1987



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for: LINDA HURDLE STOCKDALE BREWER  
Director

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<sup>1</sup>In this proceeding, Michael J. Siegel represented himself. The BDCFC was represented by Gus Skarakis, the BHF, by Anita Scuri, both with the Department of Consumer Affairs.

<sup>2</sup>The legal background of the regulatory determination process--including a survey of governing case law--is discussed at length in note 2 to 1986 OAL Determination No. 1 (Board of Chiropractic Examiners, April 9, 1986, Docket No. 85-011), California Administrative Notice Register 86, No. 16-Z, April 18, 1986, pp. B-14--B-16; typewritten version, notes pp. 1-4. See also Wheeler v. State Board of Forestry (1983) 144 Cal.App.3d 522, 192 Cal.Rptr. 693 (overturning Board's decision to revoke license for "gross incompetence in . . . practice" due to lack of regulation articulating standard by which to measure licensee's competence); City of Santa Barbara v. California Coastal Zone Conservation Commission (1977) 75 Cal.App.3d 572, 580, 142 Cal.Rptr. 356, 361 (rejecting Commission's attempt to enforce as law a rule specifying where permit appeals must be filed--a rule appearing solely on a form not made part of the CAC). For an additional example of a case holding a "rule" invalid because (in part) it was not adopted pursuant to the APA, see National Elevator Services, Inc. v. Department of Industrial Relations (1982) 136 Cal.App.3d 131, 186 Cal.Rptr. 165 (internal legal memorandum narrowly interpreting ambiguous statute). Also, in Association for Retarded Citizens--California v. Department of Developmental Services (1985) 38 Cal.3d 384, 396 n.5, 211 Cal.Rptr. 758, 764 n.5, the court avoided the issue of whether a DDS directive was an underground regulation, deciding instead that the directive presented "authority" and "consistency" problems).

<sup>3</sup>We refer to the portion of the APA which concerns rulemaking by state agencies: Chapter 3.5 of Part 1 ("Office of Administrative Law") of Division 3 of Title 2 of the Government Code. Sections 11340 through 11356, Chapters 4 and 5, also part of the APA, concern administrative adjudication rather than rulemaking.

<sup>4</sup>The "unsecured guaranties" are described by the Department of Consumer Affairs' Deputy Director/Chief of Legal Affairs (see Exhibit A) as "little more than . . . unsecured promissory note[s]". Lacking a copy of an actual letter of guaranty in the record, we rely upon this undisputed Consumer Affairs' characterization of the documents in question.

<sup>5</sup>As we have indicated elsewhere, an OAL determination concerning a challenged "informal rule" is entitled to great weight in both judicial and adjudicatory administrative proceedings. See 1986 OAL Determination No. 3 (Board of Equalization, May 28, 1986, Docket No. 85-004), California Administrative Notice Register 86, No. 24-Z, June 13, 1986, p. B-22; typewritten version, pp. 7-8; Culligan Water Conditioning of Bellflower, Inc. v. State Board of Equalization (1976) 17 Cal.3d 86, 94, 130 Cal.Rptr. 321, 324-325. The Legislature's special concern that OAL determinations be given appropriate weight in other proceedings is evidenced by the directive contained in Government Code section 11347.5: "The

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office's determination shall be published in the California Administrative Notice Register and be made available to . . . the courts." (Emphasis added.) Implementing this directive, this and other determinations are presently being mailed to the presiding judges of all state and federal courts in California.

<sup>6</sup>In this case, no response to the Request for Determination was submitted. In general, we encourage affected agencies to submit responses in order to obtain full presentation of contrasting viewpoints. If the affected agency concludes that part or all of the challenged rule is in fact an underground regulation, it would be helpful, if circumstances permit, for the agency to concede that point and to permit OAL to devote its resources to analysis of truly contested issues.

<sup>7</sup>An OAL finding that a challenged rule is illegal unless adopted "as a regulation" does not of course exclude the possibility that the rule could be validated by subsequent incorporation in a statute.

<sup>8</sup>We discuss the affected agency's rulemaking authority (see Gov. Code, §11349(b)) in the context of reviewing a Request for Determination for the purposes of exploring the context of the dispute and of attempting to ascertain whether or not the agency's rulemaking statute expressly requires APA compliance. If the affected agency should later elect to submit for OAL review a regulation proposed for inclusion in the California Administrative Code, OAL will, pursuant to Gov. Code, §11349.1(a), review the proposed regulation in light of the APA's procedural and substantive requirements.

The APA requires all proposed regulations to meet the six substantive standards of necessity, authority, clarity, consistency, reference, and nonduplication. OAL does not review alleged "underground regulations" to determine whether or not they meet the six substantive standards applicable to regulations proposed for formal adoption.

The question of whether the challenged rule would pass muster under the six substantive standards need not be decided until such a regulatory filing is submitted to us under Gov. Code, §11349.1(a). At that point in time, the filing will be carefully reviewed to ensure that it fully complies with all applicable legal requirements.

Comments from the public are very helpful to us in our review of proposed regulations. We encourage any person who detects any sort of legal deficiency in a proposed regulation to file comments with the rulemaking agency during the 45-day public comment period. Such comments may lead the rulemaking agency to modify the proposed regulation.



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If review of a duly-filed public comment leads us to conclude that a regulation submitted to OAL does not in fact satisfy an APA requirement, OAL will disapprove the regulation. Gov. Code, §11349.1.

<sup>9</sup>Government Code section 11342(a). See Government Code sections 11346; 11343. See also 27 Ops.Cal.Atty.Gen. 56, 59 (1956).

<sup>10</sup>See Poschman v. Dumke (1973) 31 Cal.App.3d 932, 943, 107 Cal.Rptr. 596, 609.

<sup>11</sup>See Faulkner v. California Toll Bridge Authority (1953) 40 Cal.2d 317, 324 (point 3); Winzler & Kelly v. Department of Industrial Relations (1981) 121 Cal.App.3d 120, 174 Cal.Rptr. 744 (points 1 and 2); cases cited in note 2 of 1986 OAL Determination No. 1. A complete reference to this earlier Determination may be found in note 2 to today's Determination.

We also conclude that the bond waiver policy is "quasi-legislative" in nature because it is a rule formulating a general policy oriented toward future decisions. Gov. Code, §11346. See Pacific Legal Foundation v. California Coastal Commission (1982) 33 Cal.3d 158, 168, 188 Cal.Rptr. 104, 111 (quasi-legislative acts are reviewable by ordinary mandamus (Code Civ. Pro., sec. 1085) or action for declaratory relief (Code Civ. Pro., sec. 1060); whereas, quasi-judicial or adjudicatory acts are reviewable by administrative mandamus (Code Civ. Pro., sec. 1094.5).)

<sup>12</sup>By way of background concerning the state of the law on the date the Request was filed, we note that the purpose of the bond statute was to make it virtually certain that aggrieved consumers would be monetarily compensated for judicially validated claims against licensees. A surety bond is a reliable source from which to pay claims. We note the statutory alternatives to filing a surety bond: \$1000 in government bearer bonds; \$1000 in cash. Former Bus. & Prof. Code section 9547. Code of Civil Procedure section 995.710(a) provides several more alternatives for persons required to post bonds:

"(a) Except to the extent the statute providing for a bond precludes a deposit in lieu of bond or limits the form of deposit, the principal may, instead of giving a bond, deposit with the officer any of the following:

(1) Lawful money of the United States. The money shall be maintained by the officer in an interest-bearing trust account.

(2) Bearer bonds or bearer notes of the United States or the State of California.

(3) Certificates of deposit payable to the officer, not exceeding the federally insured amount, issued by banks

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authorized to do business in this state and insured by the Federal Deposit Insurance Corporation or by savings and loan associations authorized to do business in this state and insured by the Federal Savings and Loan Insurance Corporation.

(4) Savings accounts assigned to the officer, not exceeding the federally insured amount, together with evidence of the deposit in the savings accounts with banks authorized to do business in this state and insured by the Federal Deposit Insurance Corporation.

(5) Investment certificates or share accounts assigned to the officer, not exceeding the federally insured amount, issued by savings and loan associations authorized to do business in this state and insured by the Federal Savings and Loan Insurance Corporation.

(6) Certificates for funds or share accounts assigned to the officer, not exceeding the guaranteed amount, issued by a credit union, as defined in Section 14002 of the Financial Code, whose share deposits are guaranteed by the National Credit Union Administration or guaranteed by any other agency approved by the Department of Corporations."

Nowhere in either statute do we find the term "unsecured promissory note" listed as an equivalent to a surety bond "executed by an admitted surety insurer" (Business and Professions Code section 19233(a), former 9547, paragraph 1). Indeed, such an unsecured note would not effectively "obligate the surety for damages caused by the licensee to a claimant who is within a class of persons protected by the code provisions under which the bond was written." Walton v. March Fong Eu (1983) 143 Cal.App. 403, 409, 191 Cal.Rptr. 779, 783 (finding state liable to claimant for failure to demand full amount of deposit accepted in lieu of statutorily-required surety bond). [Emphasis added.]

A second arguable interpretation of former Bus. & Prof. Code section 9547 (in contrast to that followed in the text) is that the Board was free to waive the surety bond without the need for spelling out any conditions in regulation. However, under Government Code section 11342(b), such a clarifying interpretation is a standard of general application adopted to interpret a statute enforced by the Board and is thus still violative of Government Code section 11347.5. In short, insofar as the Board could have legitimately interpreted the former bond statute as not requiring "conditions" articulated in formal regulations, that latter interpretation itself could have been issued only in a regulation.

As of January 1, 1987, with the adoption of Bus. & Prof. Code section 19233(g), it became clear that the enforcing agency could accept unsecured guaranties--but only if "authorized" by formal

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regulations:

<sup>13</sup>The following provisions of law may also permit agencies to avoid the APA's requirements under some circumstances, but do not apply to the case at hand:

- a. Rules relating only to the internal management of the state agency. Government Code section 11342(b).
- b. Forms prescribed by a state agency or any instructions relating to the use of the form, except where a regulation is required to implement the law under which the form is issued. Government Code 11343(b).
- c. Rules that "establish[ ] or fix[ ] rates, prices or tariffs".
- d. Rules directed to a specifically named person or group of persons and which do not apply generally throughout the state. Government Code section 11342(b).
- e. Legal rulings of counsel issued by the Franchise Tax Board or the State Board of Equalization. Government Code section 11343(a)(3).
- f. Contractual provisions previously agreed to by the complaining party. City of San Joaquin v. State Board of Equalization (1970) 9 Cal.App.3d 365, 376, 88 Cal.Rptr. 12, 20 (sales tax allocation method was part of a contract which plaintiff had signed without protest); see Roth v. Department of Veterans Affairs (1980) 110 Cal.App.3d 622, 167 Cal.Rptr. 552 (dictum); Nadler v. California Veterans Board (1984) 152 Cal.App.3d 707, 719, 199 Cal.Rptr. 546, 553 (same); but see Government Code section 11346 (no provision for non-statutory exceptions to APA requirements); see International Association of Fire Fighters v. City of San Leandro (1986) 181 Cal.App.3d 179, 182, 226 Cal.Rptr. 238, 240 (contracting party not estopped from challenging legality of "void and unenforceable" contract provision to which party had previously agreed); see Perdue v. Crocker National Bank (1985) 38 Cal.3d 807, 821, 171 Cal.Rptr. 604, 612 ("contract of adhesion" will be denied enforcement if deemed unduly oppressive or unconscionable).

The above is not intended as an exhaustive list of possible APA exceptions.