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18 Securities Breach
BY NADER PAKFAR, KELSEY THAYER, AND KARLI BAUMGARDNER
Since 2008, courts have tended to interpret CMBS agreements strictly, allowing for even harmless breaches to trigger full recourse.

23 Homes away from Home
BY VANJA HABEKOVIC
Corporate structures may be used to address income and property tax considerations in a foreign person’s purchase of California residential real estate.

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28 Boundary Issues
BY ANDREW R. HENDERSON
Real estate buyers should be aware that under the agreed boundary doctrine, recorded lot lines may be relocated.
Statistics paint a dismal picture of the L.A. housing market. In August 2015, the UCLA Luskin School of Public Affairs released a study titled “Impacts of the Widening Divide: Why Is LA’s Homeownership Rate So Low?” Its authors point out that “The Los Angeles metro area…has the lowest homeownership rate among metropolitan areas in the U.S.” The percentage of homeowners in this county is 46, while in New York City it is 52 percent and 54 percent in the Bay Area. It is also considerably below the national average of 64 percent. In addition, the UCLA study comments that the metropolitan statistical area of Los Angeles “has the highest average housing burden and new owner costs.”

Local renters face an increasing financial burden too. In a press release published last August, Zillow indicates that in the second quarter of 2015 local tenants paid 48.9 percent of their income in rent, as opposed to 35.6 percent between 1985 and 2000. In contrast, in the New York-Northern New Jersey area the percentage is 41.3. Whatever the city, more dollars spent on rent means less to buy groceries, pay car expenses or Metro fares, obtain insurance, and have a little left over for discretionary activities or savings.

A variety of factors have contributed to this housing crisis. Stagnant wages is a key one. As a Los Angeles Times editorial, “How to get more affordable housing in Los Angeles,” observed in August 2015 that “Housing prices in Los Angeles have grown four times faster than incomes since 2000.” Similarly, the UCLA study cited above notes, “Since 1970, renters in Los Angeles, particularly those in the bottom income quartile, have been severely burdened, paying more than 30% and increasingly 50% of their income in rents.”

Land use regulations also play a significant role. As planner and professor Gregory D. Morrow described in a Los Angeles Times op-ed piece last July, “For much of the last 40 years, planning in Los Angeles has been guided by the idea that growth is bad, that more people mean more congestion, pollution and social ills. The city has emphasized ‘downzoning’—reducing the number of units allowed to be built on properties—to actively curb growth. It hasn’t worked.…since 1970, half a million more people have moved to Los Angeles than were planned for…."

With 2016 being an election year, the forecast is for continued hand wringing by candidates about the Los Angeles housing crisis. Once the electorate has spoken in November and public officials feel momentarily motivated to demonstrate a capacity to act, perhaps the scarcity of new housing development initiatives will be replaced with those actually leading to more affordable single-family homes and apartments being built. This includes adoption of local inclusionary zoning ordinances for market-rate residential developments and adoption of state and federal tax incentives to promote housing. For those looking for a clean, decent, safe place to put their feet up after a hard day at work, the hope is that speeches are replaced with real change beginning now.
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Daniel M. Grigsby General Counsel of the Los Angeles Lakers

Before moving in-house as general counsel, Daniel M. Grigsby served as outside counsel to the Lakers for more than 32 years, most recently as a partner with Jeffers Mangels Butler & Mitchell, where he served as chairman of the firm’s national sports law group.

What is the perfect day? Winning another NBA championship for the Lakers!

What are your main job duties as general counsel for the Lakers? Player contract matters, sponsorship and broadcast matters, and general business. I truly am a general counsel.

What’s new? We bought a piece of land in El Segundo where we will build a 120,000-square-foot, state-of-the-art training center and office building. It should be completed in June of 2017.

Why move? Several reasons. First of all, player recruiting. Players today want to know what amenities we have, what kind of workout, recovery, and nutrition facilities we have. Second is that we currently operate out of three different office buildings.

Has the game changed? Players all have their own brand. They want a place that is social-media friendly and that allows them to best prepare for their playing careers.

Are players injured more than before? Athletes today play year round, which puts tremendous stress on their bodies. Arthroscopic surgery is more commonplace in the off season to treat injuries caused by repetitive stress.

Do you think certain athletes are more injury-prone than others? The true giants, the bigger guys, 300 pounds, jumping and landing—yes, it’s the way they are built. But training has improved too.

How has the loss of Dr. Buss impacted the Lakers? Losing someone of his intelligence, experience, and vision was tough, but he did a good job of prepping everyone for life after Dr. Buss.

What is the biggest legal challenge facing the NBA? The NBA just signed a major national television deal which will pay approximately $25 billion over the next eight seasons. It more than doubles the revenues that each team will receive from national TV, which in turns drives the salary cap up because currently players get roughly 51 percent of basketball-related income. Rather than players signing new, long-term five-year deals, they are signing shorter deals to see what happens.

Is it harder to build a dynasty now? Yes. We hear all the time, “Why don’t you get player ‘A’ and player ‘B’ and add them to Kobe?” But the salary cap rules prevent teams from doing that.

Does it make sense that different sports have different salary restrictions? Yes, I think they’ve gotten it right for the individual sports. The NBA system works pretty well, it has a “soft” cap with some exceptions and a progressive luxury tax for those exceptions. Baseball is a free market, with a luxury tax. Football has a hard cap.

The reasons for each system are inherent in the nature of the sports to which they apply.

Are you in favor of “one and done”? I think the league and NCAA teams would like to have it be two years. I’m a college basketball fan; I’m a Bruin. It’s tough on colleges to have someone for one year and lose them.

Why should a tennis player be able to turn pro at 13 and a basketball player have to wait? Tennis players are individual athletes, and their entourage probably includes their parents and a private coach that their parents have hired. It’s a little different in basketball. Bringing in most 19-year-old kids, paying them significant amounts of money, and putting them in with grown men in their late 20s to early 30s—they have to grow up pretty fast. The league has an extensive transition program, and the players are required to go.

Do you think it’s appropriate for the league to own a team? Probably not, but sometimes there is no choice, as was the case with New Orleans a few years ago.

Were you an athlete? I played for the Kansas City Royals Baseball Academy for a few weeks back in 1972 and I realized I was only an adequate player. I played basketball in high school.

What is your favorite spectator sport? Basketball. But, I also really enjoy baseball. If you understand baseball, it is like a big chess game going on all the time.

What do you do on a perfect three-day weekend? Golf on Saturday morning and in the evening, go out with my wife and friends for cocktails and dinner. Sunday morning is church, and Sunday afternoon, basketball or baseball.

What are your favorite vacation spots? Cabo and Oahu. I’m a Waikiki fan because of the great mix of being in paradise but having great restaurants, shopping, and
other activities nearby. One of my favorite spots to relax is under the giant banyan tree at the Moana Surfrider.

Any advice for law school students who want a job like yours? Get into the best law school you can, do the best that you can while there, take all of the IP courses you can, and if you can, write sports-related articles for law review. If you clerk or work while in school, try to find something related to sports. You need to distinguish yourself from thousands of other students who want work in sports law.

Has the business changed? According to Forbes, the Lakers are worth at least $2.6 billion. The Lakers are a brand. We can’t make enough money selling out the Staples arena at whatever price we can charge to even pay our players. At the end of the day, we are a global trademark and brand.

Do you have a favorite jersey? Growing up, I was always a Jerry West fan. More recently, I am a Kobe Bryant fan because no one works harder than Kobe.

Do you think the NBA will ever change its Jerry West logo? No. And they shouldn’t. It’s iconic.

What would you grab while running out of the front door if your house were on fire? My family, my pets, and pictures.

How do you get your news? Lots of sources. I read the Los Angeles Times every morning, from cover to cover, and SportsBusiness Journal.

What television shows do you record? Homeland, Blacklist, Quantico. Mostly political dramas.

What is your favorite movie? Field of Dreams—having lost my father at a young age and being a baseball player, the scene at the end where he asks his dad, “Do you want to have a catch?” gets me every time.

What are the three most deplorable conditions in the world? People killing each other in the name of religion, global hunger, and imperialism.

Who are your two favorite U.S. presidents? Ronald Reagan and John Kennedy both had the courage of their convictions and went against the grain. Perhaps that got Kennedy killed.

What is the one word you would like on your tombstone? Only one? Warrior.
Enforcing No-Contest Clauses in the Face of Anti-SLAPP Motions

A STRATEGIC LAWSUIT against public participation (SLAPP) is a malicious or frivolous cause of action intended to chill the valid exercise of First Amendment rights. California’s anti-SLAPP statute provides for a special motion to strike any cause of action arising from the exercise of the rights of petition and free speech. Recently, trust and estate litigators have been turning to anti-SLAPP motions to attack petitions to disinherit beneficiaries under no-contest clauses, with twofold consequences: 1) parties seeking to disinherit a beneficiary for violating a no-contest clause must meet a higher evidentiary burden before proceeding to the fact-finding stage, and 2) parties must endure delays while the anti-SLAPP issues are decided and appealed.

In probate court, a beneficiary may bring an anti-SLAPP motion to strike an adversary’s petition to disinherit him or her under a no-contest clause. Anti-SLAPP analysis entails a two-step inquiry: if the beneficiary establishes that the adversary’s cause of action arises from the beneficiary’s protected activity, the burden shifts to the adversary to demonstrate its probability of prevailing on the underlying petition to disinherit. If the adversary fails to meet this burden, the court will strike the petition.

A beneficiary has much to gain by filing an anti-SLAPP motion in response to a petition to disinherit under a no-contest clause. Because any petition to disinherit based on a beneficiary’s challenge to a testamentary instrument necessarily arises from the challenge (an exercise of the beneficiary’s right to petition), the beneficiary will have a strong argument that the first prong of the anti-SLAPP analysis is satisfied. In a recent decision, Rosenberg v. Reid, the court of appeal acknowledged that “actions to enforce a no-contest clause will...in many cases arise from protected activity under the anti-SLAPP statute.” Although the Rosenberg court did not explicitly recognize that all actions to enforce a no-contest clause will satisfy the first prong of the anti-SLAPP analysis, this conclusion can be inferred from the court’s reasoning for affirming the applicability of the anti-SLAPP statute. Responding to the defendant’s argument that applying the anti-SLAPP statute to her petition “would in effect render all valid No Contest clause enforcement actions SLAPPs,” the court explained that this effect “hardly seems excessive” because the second prong of the anti-SLAPP test ensures that only meritless pleadings will ultimately be stricken. Thus, a beneficiary’s adversary will likely be forced to demonstrate a probability of prevailing at the outset to avoid having its petition stricken.

This situation confers at least three strategic advantages on the beneficiary: 1) the beneficiary’s adversary may be unable to prove a probability of prevailing at such an early stage and with limited discovery, 2) in any event, the beneficiary’s adversary must tip its hand by revealing its supporting evidence, and 3) the beneficiary’s anti-SLAPP motion will effect a delay in the proceedings—filing an anti-SLAPP motion stays all discovery relating to the petition to disinherit, and the trial court’s decision on the anti-SLAPP motion is immediately appealable. Moreover, while the party opposing the anti-SLAPP motion must demonstrate the motion was “frivolous” or “solely intended to cause unnecessary delay” to recover attorney’s fees and costs, the beneficiary is entitled to fees and costs simply for prevailing on the motion.

Consequently, litigators should keep the following practical considerations in mind when seeking to enforce or defend against the enforcement of a no-contest clause. On one hand, a beneficiary filing a challenge that might trigger a no-contest clause should be prepared to file an anti-SLAPP motion if another party files a petition to disinherit. The beneficiary should file this motion quickly to halt discovery and force the adversary to make the required evidentiary showing based on limited information. On the other hand, the beneficiary’s adversary should only file a petition to disinherit once he or she is prepared to demonstrate a probability of prevailing. Indeed, the adversary could wait until the beneficiary’s contest is fully litigated before bringing a petition to disinherit so the beneficiary would no longer have grounds to argue that the petition curtails his or her right to petition the court.

Although the legislature likely did not foresee that the anti-SLAPP statute would be applied to no-contest clause enforcement proceedings, this procedure is a recurring reality today. Thus, until the legislature or courts intervene, litigators either filing or opposing a petition to disinherit a beneficiary under a no-contest clause should be aware of the implications of anti-SLAPP’s application in this context so that they are better positioned to advance and protect client interests. ——

3 Navelier v. Sletten, 29 Cal. 4th 82, 89-90 (2002). The second prong of anti-SLAPP analysis “operates like a motion for summary judgment in reverse.” Grewal v. Jammu, 191 Cal. App. 4th 977, 990 (2011). The plaintiff need only “demonstrate that the complaint is both legally sufficient and supported by a sufficient prima facie showing of facts to sustain a favorable judgment...” Oasis West Realty, LLC v. Goldman, 51 Cal. 4th 811, 820 (2011). “If the plaintiff can show a probability of prevailing on any part of its claim, the cause of action is not meritless and will not be stricken.” Id.
5 Id., citing Navelier, 29 Cal. 4th at 93-94.
6 Code Civ. Proc. §425.16(g).
7 Code Civ. Proc. §425.16(i).
8 Code Civ. Proc. §425.16(c)(1).

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Wireless communication has become a critical infrastructure, alongside water, gas, and electricity. Despite the recent rise of wireless technology, its connectivity relies on the old legal principles of real estate. To satisfy the fast-growing demand for connectivity, major wireless carriers such as AT&T, Sprint, T-Mobile, and Verizon must not only maintain but continue to expand an infrastructure of cell towers and other telecommunication facilities that occupy land.

Wireless communication is developing so quickly that even a recent basic overview of the various land use requirements of cell tower siting and network infrastructure is due for an update. Notwithstanding a congressional mandate provided in 2012, the process of wireless facility siting has remained burdensome and time consuming. Accordingly, more recent developments at the federal and state level have further streamlined the siting process. These new developments determine what types of wireless projects qualify for streamlined treatment, distinguish clear areas from gray, identify the law’s limitations, and propose an outlook on the future of wireless deployments under the new laws.

Much like zoning for any other real estate development, wireless facility siting is primarily handled at the state and municipal level. However, federal law may sometimes preempt conflicting municipal law. For example, the 2012 Spectrum Act provides that a local municipality “may not deny, and shall approve” an “eligible facilities request” for the modification of an “existing” wireless “tower” or “base station” that does not “substantially change” the physical dimensions of the tower or base station.

At first blush, the Spectrum Act offers favorable relief to wireless siting applicants seeking certain entitlements from any given municipality by providing the municipality “may not deny, and shall approve” an application over which the municipality previously may have enjoyed the ability to exercise discretion. Indeed, when a municipality’s zoning code requires a lengthy or discretionary process, this federal law may mandate the municipality take a different course of action.

However, many of the act’s terms, such as “eligible facilities request,” “existing,” “tower,” “base station,” and “substantially change,” were not defined. The wireless industry applicants and the local jurisdictions often did not agree on when the act was applicable. Recently, the FCC, which is charged with ensuring that communication infrastructure can be rapidly and efficiently deployed, provided the wireless industry with relief by issuing an order (FCC Order) and rulemaking designed to significantly streamline certain wireless infrastructure deployments.

Eligible Facilities Request

The Spectrum Act provides that an “eligible facilities request” refers to any project that involves the collocation, removal, or replacement of transmission equipment. The FCC has clarified that the act’s wireless siting rules—often referred to as Section 6409 provisions—may apply to a wide range of projects, including antenna modifications, the addition of new fiber optic lines and generators, the placement of the first wireless facility on an existing building or other structure, and even certain tower enhancements. These types of site enhancements are critical to ensuring wireless facilities are updated to keep up with new mobile device technology, ever-expanding consumer demand, and public safety needs. The wholesale removal and replacement of a tower, however, falls outside the scope of Section 6409.

“Existing” wireless towers or base stations refer to infrastructure that has been previously reviewed and approved under the applicable local zoning process or that has received another form of affirmative state or local regulatory approval, such as from the state public utility commission. Facilities placed as a matter of right, those not required to undergo a siting review at the time constructed, or facilities deployed without proper review do not qualify as “existing” towers for the purposes of Section 6409.
Section 6409 does apply to modifications and additions to 1) “towers,” defined as any structure built for the sole or primary purpose of supporting an FCC-licensed or authorized antenna and its associated equipment, regardless of whether the antennas and associated equipment are located on the tower and regardless of whether the tower has actually been constructed, and 2) a wide variety of “base station” structures, such as buildings, water tanks, utility poles, or light standards, so long as the structure supports antennas or associated equipment at the time the application is filed.12

In determining whether a project will result in a “substantial change,” six factors will be evaluated: 1) changes in height, 2) changes in width, 3) increase in the number of equipment cabinets, 4) deployment or excavation activity outside the existing footprint of the site, 5) defeat to existing concealment measures, and 6) compliance with the conditions of prior approvals.13 In order to ensure streamlined review and to ensure the municipality can require as part of the zoning application, 2) how long the municipality can take to rule on an application covered by Section 6409, review it, and 3) what happens when the municipality cannot request new information out of the scope of its original request.25

Under the shot clock requirements, reasonable response times have historically been defined as 90 days for site modifications and collocations and 150 days for a new cell site, unless otherwise agreed between the parties.18

The FCC clarified that the 90- or 150-day shot clock timelines apply only to zoning applications falling under Section 332 of the Telecommunications Act of 199619 and imposed a new, shortened shot clock period of 60 days for the review of applications falling under Section 6409.20 If a jurisdiction fails to rule on an application covered by Section 6409 within the new 60-day shot clock period (accounting for tolling), the request will be deemed granted.21 This approval only takes effect after the applicant submits written notice to the municipality that the approval time period has elapsed and during that time the municipality did not take definitive action on the zoning application.22

In the event the municipality disagrees with this determination, the burden shifts to the municipality to seek relief in the courts rather than the applicant having to seek this remedy, as is the case with zoning applications submitted under Section 332. This “deemed granted” remedy alone may result in a significant acceleration of deployment projects and is a welcome relief for carriers, most of which are reluctant to sue the local authorities for every violation of the shot clock.

In addition to imposing a new shot clock for Section 6409 applications, the FCC also clarified how and when the shot clock applies. First, the shot clock begins to run when an application is submitted, not when it has been deemed complete by the municipality.23 Second, in the event that a municipality deems the application incomplete, the municipality has 30 days to request the missing information, and it must also identify the code section or publicly stated requirement that requires the missing information.24 Third, when the applicant resubmits the requested application materials, the local authority has 10 days to identify which previously requested pieces of information are still missing, and the municipality cannot request new information outside the scope of its original request.25

This prescribed shot clock scheme prevents municipalities from asserting serial requests for supplemental documentation and information, which would effectively string together multiple tolling periods to artificially elongate the shot clock approval timeframe. The FCC also declared that the shot clock will run regardless of any local moratorium on zoning approvals of wireless facilities.26 These shot clock administration guidelines apply to zoning applications submitted under either Section 6409 or Section 332.

Unfortunately, the FCC stopped short of changing the effect of a municipality’s failure to meet the Section 332 shot clock timelines. Any disputes regarding a local authority’s failure to meet the Section 332 shot clock must be resolved in court. Also, the municipality maintains its right to request extraneous project information—for example, traffic studies, development impact reports, or copies of the underlying lease or other owner consent documents.27

DAS and Small Cells

The FCC has confirmed that the deployment of smaller-scale facilities known as distributed antennas systems (DAS) and small cells may qualify for the protections of Sections 332 and 6409.28 Further, in light of the smaller nature and therefore lessened impact of these installations on the environment, the FCC has created new categorical exclusions from environmental and historical review for many of these minimally obtrusive facilities.

Qualifying interior facilities, collocations, and facilities in the rights-of-way will no longer need either an Environmental Assessment (EA) or Environmental Impact Statement (EIS) as to the potential impacts of the project under the National Environmental Policy Act of 1969 (NEPA).29 Specifically, the FCC extended the existing NEPA categorical exclusions for antenna collocations on buildings and towers to include equipment associated with the antennas, such as wiring, cabinets, backup power equipment, and collocations in a building’s interior.30 This NEPA categorical exclusion for collocations was also extended to collocations on structures other than buildings and towers.31 Further, the FCC created a categorical exclusion for projects that will not result in a substantial increase in size over the existing utility or communications uses of 1) the public right-of-way designated for communication towers, 2) above-ground utility transmission lines, or 3) any associated structures and equipment.32

Similarly, qualifying collocations on utility poles and transmission towers33 (but not light standards) and qualifying collocations on buildings and certain nontower structures34 will not require consultations with the State Historic Preservation Officer (SHPO), Tribal Historic Preservation Officer (THPO), or Advisory Council on Historic Preservation (ACHP) as otherwise required under the National Historic Preservation Act of 1966 (NHPA, also known as Section 106).35 In order to qualify for this exclusion and preserving no other exclusions otherwise apply, the collocated equipment, when measured with any other wireless deployment on the same structure, must meet certain size and ground disturbance limitations.36 Lastly, any structure can now qualify for Section 106 exclusion, regardless of age—even if older than 45 years.37
Finally, the FCC ruled that the existing exclusions for certain collocations on buildings under FCC programmatic agreements are now extended to collocations inside buildings. The FCC has already begun discussions about broader reforms to expedite applicable DAS and small cell wireless facilities deployments and relieve all stakeholders of unnecessary and nonproductive obligations. These discussions are anticipated to conclude in 18 to 24 months, at which time new reforms will be announced.

The FCC Order has been challenged by Montgomery County, Maryland; the California cities of Los Angeles, San Jose, Redwood City, and Ontario; the city of Bellevue, Washington; the city of McAllen, Texas; and the Texas Coalition of Cities for Utility Issues in an appeal pending before the Fourth Circuit Court of Appeals. These petitioners have limited their challenge to those portions of the FCC Order implementing Section 6409. Petitioners claim the FCC overreached its rulemaking authority, resulting in a violation of the Tenth Amendment. A stay pending appeal was not sought by the petitioners, and all parts of the FCC Order remain in effect.

**State Law**

While the FCC Order imposed a “deemed granted” remedy for certain collocations and minor modifications that do not result in a substantial change (i.e., eligible facility requests), the commission was unwilling to extend this remedy to other collocations, new sites builds, or major modifications. However, the California State Legislature has now filled this gap by extending a “deemed granted” remedy to these siting applications as well. Following the FCC Order, California State Assemblyman Bill Quirk introduced Assembly Bill 57, addressing land use approvals of wireless telecommunication facilities. The bill was passed by large majorities in the Assembly and the Senate despite intense lobbying efforts by local governments and their affiliated organizations.

Effective January 1, 2016, AB 57 added Section 65964.1 to the Government Code, which provides that wireless communications facility collocation or siting applications not acted on in a dispositive manner by a city or county within the reasonable time periods established by the FCC (90 days for collocations and 150 days for other applications) will be “deemed approved.” This new law would allow a “deemed approved” remedy only if all public notice requirements regarding the application for the wireless telecommunications facility have been met, and the applicant has provided a notice to the city or county that the reasonable time period has lapsed. The applicable review time frame can be tolled to accommodate timely requests for information required to complete the application or by mutual agreement between the applicant and the local government. Section 6409 “eligible facility requests” for minor modifications to existing facilities, described above, fall outside the projects covered by AB 57 and remain subject to the new FCC 60-day shot clock. AB 57 also does not extend to telecommunication projects proposed on fire department facilities. Once a siting application has been deemed approved, the city or county will have 30 days to file a court action challenging the deemed approved status and stop the construction. By enacting this legislation, California joins with a growing number of other states—including Georgia, Indiana, and Iowa—in passing laws aimed at accelerating upgrades to wireless infrastructure in an effort to meet the demands of an ever-growing base of consumers.

In light of the framework established by the new federal guidance and new state law, wireless carriers will be closely tracking the date siting applications are submitted, the date notifications of application incompleteness are issued, and any shot clock tolling periods and expirations. Carriers will be pushing to move forward with siting applications that have been deemed granted or approved under federal or state law. However, it may take considerable time for municipalities to update their codes and application forms to align with the new requirements. In the meantime, certain progressive municipalities work cooperatively with applicants to achieve a solution that not only accommodates the streamlined approach required by law but also complies with municipal code as it relates to wireless deployments. For example, jurisdictions with codes that require public hearings for siting applications arguably falling under Section 6409 are endeavoring to hold the hearing and issue approvals within the 60-day shot clock period.

Although much progress has been made, much work remains to be done to meet the steadily growing demand for wireless communication infrastructure. Carriers and municipalities can work together to find solutions to support the efficient and balanced deployment of wireless infrastructure, which benefits not just the wireless industry but all who have come to rely on smartphones and other devices (such as those now found in cars) that employ wireless communication technology.

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1. See Lynn Whitcher & Cynthia Hanson, Tower Building, Los Angeles Lawyer 30-34 (Jan. 2014).
6. The FCC ruling also has implications extending beyond wireless (including to public safety, broadcast, and WiFi).
7. FCC Order, supra note 3.
10. See 47 C.F.R. §1.40001(b)(4).
12. See 47 C.F.R. §1.40001(b)(1), (9).
18. See 80 Fed. Reg. 1259 (In the FCC’s 2009 Declaratory Ruling, the commission interpreted a “reasonable period of time” under §332(c)(7)(B)(ii) to be 90 days for processing collocation applications and 150 days for processing applications other than collocations.).
20. See 47 C.F.R. §1.40001(c)(2).
21. 47 C.F.R. §1.40001(c)(4).
22. 47 C.F.R. §1.40001(c)(8).
23. 47 C.F.R. §1.40001(c)(3).
24. 47 C.F.R. §1.40001(c)(3).
25. 47 C.F.R. §1.40001(c)(3).
26. 47 C.F.R. §1.40001(c)(3).
27. See generally 47 U.S.C. §332(c)(7).
30. See id.
34. Collocations on a building or other nontower structure are excluded from Section 106 review to the extent not otherwise already excluded if 1) there is an existing antenna on the building or structure, 2) antenna proximity requirements are met, 3) the new antenna(s) will comply with all zoning conditions and historic preservation conditions imposed on existing antennas that mitigate or prevent environmental impact (such as stealthy requirements), and 4) they meet ground disturbance requirements. These criteria apply to equipment collocated within a building as well as on its exterior.
35. The Texas Coalition of Cities for Utility Issues.
36. See Lynn Whitcher & Cynthia Hanson, Tower Building, Los Angeles Lawyer 30-34 (Jan. 2014).
41. Gov’t Code §65964.1(a).
42. Gov’t Code §65964.1(a)(2).
44. Gov’t Code §65964.1(a)(1).
45. Gov’t Code §65964.1(f).
46. Gov’t Code §65964.1(3)(B).
The Effect of *Brisbane* on the Construction Defects Statute of Limitations

FOR THE REMAINDER OF 2016, the 1997 edition of the *General Conditions of the Contract for Construction*,¹ published by the American Institute of Architects (AIA) and typically incorporated into the AIA standard form prime agreement between an owner and contractor, contains language that has been adjudicated to circumvent the Code of Civil Procedure’s statute of limitations scheme and the delayed discovery rule in favor of a party-negotiated limitations period that time-bars all claims four years after the notice of completion. However, the clock is ticking as this defense will evaporate after December 31.

In *Brisbane Lodging, L.P. v. Webcor Builders, Inc.*, the California Court of Appeal upheld the enforceability of a provision of a standardized contract form promulgated by AIA that waived the application of the delayed discovery rule to an action for a latent construction defect claim.² The contract between Brisbane and Webcor contained the 1997 AIA standard form of agreement between owner and contractor (cost plus fee) and document A201 general conditions (AIA A201). By agreement between the parties, Article 13.7.1.1 of AIA A201 establishes a contract-based limitations scheme and abrogates the delayed discovery rule. At the end of 2016, the extent to which *Brisbane*’s abrogation of statutory rights and the common law rule disappear as the 1997 edition of A201 has been revised and superseded by the 2007 edition. Whereas *Brisbane* relied on the 1997 edition of AIA A201, the critical language of Article 13.7.1.1 was modified to all but eliminate the present opportunity to assert a claim as time-barred by the 1997 edition of the AIA A201.

In ruling that Brisbane’s claim against Webcor was time-barred, the court of appeal recognized the right of sophisticated parties to waive the statute of limitations contained in the Code of Civil Procedure in favor of those provided by a form contract. The decision legitimizes the use of the standardized AIA A201 General Conditions in California. At the same time, the *Brisbane* court was not required, nor asked, to resolve the possible effect of this negotiated limitations period on express or equitable indemnification causes of action as part of their case on appeal, and there is presently no clear answer as to whether or not *Brisbane* also abrogates such indemnification causes of action that arise out of the project at issue.

Established in 1857, the AIA publishes widely accepted standard form agreements for a multitude of contractual relationships. The first common use contract was circulated by the AIA in 1888, and the first standardized General Conditions were published in 1911.³ The General Conditions have become, and are recognized as, a substitute for portions of the California Commercial Code.⁴ They are ubiquitous in the owner-architect, design, construction management, and general contracting industries and are regularly relied upon by governments, architects, owners, and construction industry professionals.⁵

In *Brisbane*, a property owner contracted with a builder for the construction of a hotel, which was substantially completed on July 31, 2000. In January 2005, the owner discovered a broken sewer line. The builder visited the site in March 2005 and concluded that the sewer line break was a latent defect for which the plumbing subcontractor was responsible. In July 2005, the plumbing subcontractor made repairs to the kitchen sewer line. In October 2007, while inspecting another plumbing problem under the structure, the plumbing subcontractor discovered that the pipe sections had become disconnected. No repairs were made, nor was the owner informed of the plumber’s discovery.

In May 2008, Brisbane sued Webcor for breach of contract, negligence, and breach of implied warranties. The builder moved for summary judgment, contending that the entire action was time-barred by Article 13.7.1.1 of the AIA A201 General Conditions because A201 provides that the statute of limitations began to run on the date of substantial completion.⁶ The owner opposed the motion, contending “(1) it had never agreed to waive its right to sue for ‘latent’ defects; (2) Article 13.7.1.1 was too vague to be interpreted as a waiver of the provision of section 337.15, which sets a maximum 10-year period to sue for latent defects; and (3) a clause purporting to abrogate the delayed discovery rule would be against public policy.”⁷ The trial court granted the builder’s motion, and the appellate court affirmed.

The statutory basis for the owner’s opposition is founded upon Sections 337.1 and 337.15 of the California Code of Civil Procedure, which set a four-year statute of limitations and a 10-year statute of repose, respectively, upon an aggrieved party that seeks to recover damages from one who “performed or furnished the design, supervision, or observation of construction or construction of an improvement to real property.”⁸ These statutes provide that, in most circumstances, the claim accrues on the date of a substantial completion of the project. However, when a construction defect is latent or otherwise undiscoverable without investigation as of the date of substantial completion, this bright-line rule can produce inequitable results by precluding a latent defect claim that is actually discovered more than four years after substantial completion. In *Brisbane*, the March 2005 discovery of the latent pipe failure would have been time-barred under a strict interpretation of Section 337.1 because it was discovered five years after the substantial completion of the project, an arguably harsh result for a party unaware of the defect giving rise to the claim.

Exceptions to this bright-line rule have developed judicially to limit this harsh result. In *Leaf v. City of San Mateo*,⁹ a property owner purchased a duplex in 1972 and later sued the developer-builder-seller for construction defects after the property owner discovered the property subsidence resulted from an improperly constructed water drainage system. The plaintiff settled with the defendants in June 1976 and used the settlement proceeds to make repairs.

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During the repair effort, the property owner discovered the city had failed to properly compact the soils covering the sewer lines on his property. These ill-compacted trenches directed groundwater underneath the property. The property owner sued the city in November 1976—13 years after completion. The city’s motion of summary adjudication was sustained, as the claim was filed more than 10 years after substantial completion in violation of Section 337.15. On appeal, the court recognized the harshness of “depriving a plaintiff of a cause of action before they were aware they had been injured.”10 The court further reasoned that before the property owner excavated around his property to effectuate the repairs attendant to the first lawsuit, he was unaware of the full extent to which he had been damaged. The court applied the delayed discovery rule, and plaintiff’s suit was restored.

The result in Brisbane turned on the interpretation of the provisions contained in the AIA 201 General Conditions. The Brisbane court engaged in a detailed examination of these provisions and concluded that Article 13.7, which is entitled “Commencement of the Statutory Limitations Period,” supersedes California’s statutory limitations period for construction defects. As drafted, Article 13.7 establishes a strict four-year limitations period for “any alleged causes of action” as of the date of “substantial completion” for a construction project. Specifically, Article 13.7, subsection 1.1 provides that for claims arising from acts or omissions before “Substantial Completion, any applicable statute of limitations shall commence to run and any cause of action shall be deemed to have accrued in any and all events not later than such date of Substantial Completion.”11

In construction defect matters, the four-year limitations period found in Article 13.7 is materially consistent with the operative terms of Section 337.1 of the California Code of Civil Procedure. However, the harsh effects of the substantial completion trigger date of Section 337.1 have been mitigated by the delayed discovery rule. Leaf and other cases have articulated that when properly applied this rule delays the substantial completion trigger to a time when the plaintiff discovers or has reason to discover the cause of action.12 Since the property owner’s latent defect claim in Brisbane did not arise until it was discovered in 2005, it was statutorily time-barred by Section 337.1. However, the claim would have survived by the application of the delayed discovery rule. Interestingly, the Commentary on Document AIA A201-1997 specifically states that the purpose of Article 13.7 is to eliminate the delayed discovery rule.13 Surprisingly, before Brisbane there had been no judicial examination or reconciliation of the differences between the Article 13.7 triggering event, which is set on the date of substantial completion, and the common-law tolling of the limitations period until the construction defect is, or could have been, discovered—the delayed discovery rule.

Brisbane went on to examine the impact of applying such a strict triggering event to the facts presented, i.e., the substantial completion condition of Article 13.7, and found that the potentially unforgiving or harsh results were, in fact, negotiated between two sophisticated parties. For this reason, Article 13.7 is “valid, enforceable and not contrary to public policy.”14 In reaching its opinion, the Brisbane court found persuasive the Maryland case of Harbor Court Associates v. Leo A. Daly Company,15 which analyzes other states’ laws and, in doing so, recognized the right of contracting parties to contract around a statutory limitations scheme, and enforced a contractual provision that specified a cause of action between the owner and contractor commenced to run upon substantial completion of the work in accordance with the applicable statute of limitations.16 Like California, Maryland applies a delayed discovery rule, and Harbor noted that neither the courts nor the legislature of Maryland ever stated that the delayed discovery rule could not be waived by contract and displayed “considerable reluctance to strike down a voluntary bargain on public policy grounds.”17 The Harbor court also found that “[i]t is especially true where… the parties to the agreement are sophisticated business actors who sought, by contract, to allocate business risks in advance.”18 Thus, the Brisbane court’s legal reasoning was based on California’s common law and persuasive authority from Maryland to respond, and overcome, the property owner’s public policy arguments in opposition.

In the end, Brisbane held that the limitations period commenced to run on the date of substantial completion as provided in Article 13.7.1.1 and all claims (patent or latent) were required to be presented within four years from that date.19 The court further reasoned that “[t]he running of the applicable statute of limitations to a date certain, the parties…negotiated to avoid the uncertainty surrounding the delayed discovery rule for the security of knowing the date beyond which they would no longer be exposed to potential liability. [S]o [s]ubject to strike their own bargains and knowingly and voluntarily contract in a manner in which certain risks are eliminated and, concomitantly, rights are relinquished.”20

The 2007 General Conditions

Brisbane stands for the proposition that Article 13.7.1.1 of the AIA 201 General Conditions clearly and unambiguously abrogates the delayed discovery rule and the provisions of Section 337.15 of the California Code of Civil Procedure.21 A contract that properly incorporates the AIA A201 General Conditions (editions 1987 through 2007 include Article 13.7.1.1) contains an enforceable contractual abrogation of the California statute of limitations for matters that arise out of “performing or furnishing the design… supervision, or observation of construction or construction of an improvement to real property….”22

This abrogation of the otherwise enforceable limitations of the California Code of Civil Procedure in defect causes of action provides the defense bar with a powerful tool to overcome claims that were latent but discovered more than four years after substantial completion. Although the Brisbane ruling is good news for the defense bar, the bad news is that the 2007 edition of the AIA A201 General Conditions was amended, and the very language upon which Brisbane analyzed to find an abrogation had been modified to defer to the applicable law for limitations periods thus, mitigating—but more likely eliminating—the potential for conflicting results between the state’s delayed discovery rule, application of the Civil Code of Procedure, and a negotiated AIA contract between sophisticated parties. Specifically, Brisbane is predicated on the 1997 edition of the AIA A201 General Conditions, which was drafted to circumvent the delayed discovery rule,23 whereas the 2007 edition was crafted to reverse this course.

In particular, the 2007 version of Article 13.7 reads in relevant part that “[t]he Owner and the Contractor shall commence all claims and causes of action… against the other arising out of or related to the Contract… within the time period specified by applicable law, but in any case not more than 10 years after the date of substantial completion.” By referring to the applicable law, the 2007 edition of the AIA A201 General Conditions is to be read in concert with the statutory limitations period as opposed to being in conflict.

The AIA’s official commentary on the 2007 Edition explains that “As a result [of the modification], the owner will have the benefit of the discovery rule in states that follow it, but the contractor will have the benefit of knowing it will not be exposed to potential liability for more than ten years after the date of substantial completion in states that follow the discovery rule.”24 In California and at least until the end of 2016 or 10 years after the 2007 edition had taken effect, Brisbane provides an effective affirmative defense for those agreements that incorporate the pre-2007 version of the AIA A201 General Conditions. After 2016, the 2007 Edition of the AIA A201 General Conditions is incorporated in the AIA standard
form agreements. Thus, the specific contractual basis upon which Brisbane is predicated no longer applies.

There is no clear record, other than the commentary, to explain the motivations that precipitated the AIA’s repositioning in regard to Article 13.7 “Commencement of Limitations Periods” within the A201 General Conditions between its 1987 and 2007 editions. It is reasonable to conclude the AIA opted to be consistent with the applicable laws of the state in which it is applied rather than in conflict.

Notwithstanding the litigation advantage Brisbane may provide to some until 2017, there remain questions as to the absolute scope of the abrogation and whether or not a cause of action for indemnity would survive the application of Brisbane. In construction litigation it is common to encounter derivative cross-actions for indemnification between a named defendant general contractor and its subcontractor cross-defendants. California Civil Code Section 2778(2) provides: “Upon an indemnity against claims, or demands, or damages, or costs, expressly, or in other equivalent terms, the person indemnified is not entitled to recover without payment thereof.” Thus, the general rule is that the statute of limitations does not start to run on an indemnity cause of action until the claimant has suffered a loss or has been damaged. Notwithstanding the general rule, all construction claims are time-barred 10 years after substantial completion, including indemnity, unless an exception applies.

Section 337.15(c)

The 10-year statute of repose of Section 337.15(c) of the California Code of Civil Procedure excludes a cross-complaint for indemnity from the 10-year bar so long as the underlying action was timely filed. In Valley Circle Estates v. VTN Consolidated the appellate court affirmed the enforceability of the exception in Section 337.15(c), and in Sandy v. Superior Court the court held further that the original construction and the events giving rise to the indemnification cause of action must also be transactionally related to the events giving rise to the underlying cause of action. Although Valley Circle and Sandy are the seminal cases interpreting Section 337.15(c), they and their progeny rely on a single critical fact that distinguishes them from Brisbane. In both Valley Circle and Sandy, Section 337.15 was valid and enforceable, whereas the Brisbane court abrogated this statute. It is incongruous to conclude that the exception of Section 337.15(c) would survive the abrogation of the code.

This raises the question of whether a derivative cross-complaint for indemnification would be possible after Brisbane in which
AIA A201 (1987 or 1997 edition) had been properly incorporated. Abrogating Section 337.15 (and presumably its exception) undermines the ability of litigants to argue the survivability of a derivative indemnification cross-action. *Brisbane* is also distinguishable in this regard as there was no such cross-action for the court to assess. However, given the decisive language of A201 (“any claims,” “all causes of action”) and the *Brisbane* court’s championing of the rights of sophisticated parties to contract around the limitations periods, another court could expand the holding to include transactionally related, derivative cross-actions for indemnity not otherwise time-barred by the California Code of Civil Procedure. Regardless, this question too becomes moot as these contract analyses begin to rely on the revised 2007 edition of A201. Any action predicated on the 1997 edition brought after January 1, 2017, will, almost assuredly, be time-barred by the 10-year statute of repose.

As such and given that *Brisbane* involved the 1997 edition of Article 13.7, its effects will evaporate with the close of 2016. Certainly, there are thousands of completed construction projects in California that relied on an AIA standard form agreement and the incorporated A201 1997 edition. Many of which have become involved in litigation or the alternative dispute resolution process. The *Brisbane* decision could prove critical to their resolution. Additionally, the impact of *Brisbane* on derivative cross-actions for indemnification has yet to be addressed. While such an action may fall far afield of the *Brisbane* holding, the same facts do not support a conclusion that an indemnification cause of action should be precluded from the scope of the *Brisbane* holding.

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3. There have been 15 formal AIA published updates since the first revision in 1915, with the most recent revision occurring in 2007. Prior to the 1976 edition, modifications to the AIA were sporadic. Following the 1976 edition, the AIA has attempted to be more predictable with its General Condition updates.
7. *Id.*
10. *Id.* at 406.
13. According to the Commentary on AIA Document A201-1997 the statute of limitations in all jurisdictions starts when a claim has accrued. In many jurisdictions, a claim accrues when the harm caused has been discovered by the innocent party. This is called the discovery rule. These provisions eliminate the discovery rule by providing that the statute of limitations begins on the date of the contractually specified occurrence. For example, the statute of limitations begins to run on the date of substantial completion for nonconforming work performed before substantial completion, even though the nonconforming work may not be discovered until years later.
17. *Harbor*, 179 F. 3d at 150.
20. *Id.* at 1260-61.
21. *Id.* at 1263-64.
23. These provisions (13.7.1.1-3) eliminate the “delayed discovery rule by providing that statute of limitations begins on the date of the contractually specified occurrence.” *Commentary on AIA Document A201-1997*, at 96.
THE INTRODUCTION of commercial mortgage-backed securities (CMBS) financing in the 1990s ushered in a period of spectacular growth in the U.S. commercial real estate market. Between 1995 and 2005, total outstanding commercial real estate loans increased by 158 percent from $1.014 trillion to $2.618 trillion.\(^1\) In 2005 alone, over one-third of new loan issuances were CMBS. A key trait of CMBS loans is that they are nonrecourse, which means that the borrower is not personally liable for the loan upon a default. Instead, the lender’s sole recourse is to repossess the property pledged as collateral for the loan.\(^2\) To address the moral hazard of borrowers operating properties recklessly and using nonrecourse provisions as a shield against personal liability, lenders have historically included exceptions in loan documents so that the commission of certain intentional acts within the borrower’s control (commonly referred to as “bad boy acts” or “nonrecourse carveouts”) would trigger personal liability. These exceptions represented the “fundamental bargain” of nonrecourse lending: so long as a borrower does not intentionally harm the lender’s collateral, the lender will look solely to the collateral, and not to the borrower’s personal assets, for recovery.

The flood of liquidity caused by the rise of CMBS precipitated the Great Recession. As commercial real estate values plummeted, taking CMBS loans down with them in the process, lenders scrambled to preserve their collateral and deter moral hazard. Their concerns were often well-founded. In the fog of war resulting from the adversarial postcrash environment, many borrowers neglected their properties, wasting them away while misappropriating whatever income remained. Lenders naturally looked to nonrecourse carveouts for relief, and an unprecedented flurry of CMBS-related litigation ensued. Never before had practitioners and courts scrutinized these carveouts so heavily.

In the wake of the recession and accompanying litigation came the advent of “CMBS 2.0,” a new lending environment in which credit underwriting standards tightened and the use of nonrecourse carveouts expanded.\(^3\) This expansion revealed two major side effects for borrowers. First, lenders pursued aggressive and often novel legal theories to exploit ambiguities in existing nonrecourse carveouts. Second, lenders became far stricter in documenting nonrecourse loans by requiring new carveouts not seen in CMBS 1.0. Taken together, these side effects substantially broaden the scope of carveouts from traditional bad boy behavior to more innocuous acts, culminating in a thorny financing environment. Borrowers must now be vigilant not to unintentionally trigger personal liability for carveouts in their existing loan documents while ensuring that any new carveouts are narrowly tailored and in the spirit of nonrecourse financing.

Historically, real estate finance practitioners

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were in general agreement (or so they thought) as to what types of bad boy acts would lead to personal liability. Acts constituting intentional malfeasance—such as fraud, misappropriation, transferring mortgaged property, filing for bankruptcy, and violating single-purpose entity (SPE) covenants and risking substantive consolidation—were indisputable nonrecourse exceptions. For the most part, any violation of these carveouts automatically resulted in personal liability for the entire amount of the loan (i.e., “springing liability” or “full recourse”) without the need for the lender to show that it incurred actual losses.

During the early years of CMBS lending, these generally accepted carveouts were included in form loan documents but rarely tested in court. Practitioners blithely assumed that they understood the scope and potential ramifications thereof. However, to the dismay of borrowers (and to paraphrase Inigo Montoya from the movie The Princess Bride), the carveouts they kept using did not mean what they thought they meant.4 Indeed, catastrophic and unintended results stemmed from breaches of two such carveouts related to SPE covenants and transfers.5

SPE Covenants

The inclusion in loan documents of SPE (or separateness) covenants is intended to separate the assets of a borrower so that, if an entity affiliated with the borrower files bankruptcy, the borrower’s assets (i.e., the lender’s collateral) are not “substantively consolidated” with those of the bankrupt entity. Customary loan documents contain over 30 such covenants, some of which are material—e.g., prohibiting the borrower from combining its assets with those of another entity—while others are not so at all—e.g., requiring the borrower to have its own letterhead. In the aggregate, however, these covenants serve a lender’s legitimate interest in preventing substantive consolidation. If a court ultimately consolidates the assets of a borrower with those of a bankrupt entity based on breach of an SPE covenant, the borrower would be hard-pressed to argue that such a breach is not tantamount to its own voluntary bankruptcy filing, which unquestionably triggers full springing personal liability.

Absent a substantive consolidation, however, a typical borrower may justifiably doubt that a seemingly innocuous breach of a single SPE covenant would result in the same recourse penalties as a voluntary bankruptcy. After all, who really cares if a borrower does not have its own letterhead? In 2011, in the oft-cited Wells Fargo Bank, N.A. v. Cherryland Mall Ltd. Partnership case, the court relied on precedent in ruling that each individual SPE covenant is equally important and any breach thereof triggers full springing recourse.6 What was wholly unprecedented was the court’s determination that the borrower’s failure to have sufficient funds to pay its mortgage constituted a breach of the covenant to “remain solvent.”7 This insolvency breach did not cause a substantive consolidation of the borrower’s assets, nor did it arise from any intentional bad boy acts taken to harm the collateral. Rather, it was caused solely by deteriorating market conditions outside of the borrower’s control.

By essentially requiring the borrower to personally guarantee the repayment of the loan (and to contribute an unlimited amount of capital beyond the value of the property to avoid a payment default), the court abandoned the fundamental bargain of nonrecourse lending and in essence converted the loan from nonrecourse to recourse. Sufficient to say that the decision created shockwaves in the real estate finance community.8

Strictly interpreting individual SPE covenants in a vacuum, and not as a whole in the context of substantive consolidation, other courts have rendered seemingly unjust and, at times, absurd decisions. In addition to solvency covenants,9 courts have said that breaches of SPE covenants prohibiting acquisition of additional property,10 admission in writing of an inability to pay debts,11 and amendment of a borrower’s organizational documents12 would all trigger full springing recourse, even if the breaches caused no actual harm.

For example, in LaSalle Bank N.A. v. Mobile Hotel Properties, LLC, the borrower agreed to a form SPE covenant not to amend its organizational documents.13 It later did so, however, simply changing the company’s stated business purpose from the “owner-ship...of a hotel” to “[engaging in] any lawful activity.”14 This benign change did not cause either a substantive consolidation of the borrower’s assets or any other harm to the lender. Yet it did trigger personal liability, with the court stating uncompromisingly that the plain language of the carveout “means what it says.”15 Because typical CMBS loan documents contain over 30 SPE covenants, many of which are insignificant if considered individually (for example, failing to “correct a known misunderstanding about its separate identity”), borrowers face a real risk that, in the CMBS 2.0 universe, innocuous and immaterial breaches of any given SPE covenant will be enforced vigorously by lenders and interpreted strictly by courts.

Transfers of Property

Another carveout under which borrowers thought they understood their risks, but by which they ultimately got burned in unanticipated ways, involves a prohibition on transfers of property. On its face, this prohibition seems reasonable and indeed essential to the fundamental bargain of nonrecourse loans. Under a plain-English interpretation of a “transfer,”16 a borrower might reasonably assume that the intent behind the carveout is to prevent the unpermitted sale of a mortgaged property. Given that such a sale is by definition an intentional bad boy act that harms the collateral, it follows that the remedy is full springing personal liability.

Due to the expansive definitions of “transfers” and “mortgaged property” found in customary CMBS loan documents, however, CMBS 2.0 borrowers have incurred springing personal liability in scenarios that most CMBS 1.0 practitioners would have thought implausible. Specifically, the term “transfers” generally includes not only sales but also any voluntary or involuntary liens, encumbrances, pledges, assignments, easements, covenants, and other dispositions of any direct or indirect interests in a mortgaged property. And likewise, the term “mortgaged property” generally includes not only land and improvements but also easements, covenants, rights to commence or defend legal actions, leases, licenses and permits, accounts, and other types of tangible and intangible property. Allowing lenders to exploit the breadth of these definitions, courts have upheld full personal liability for triggers as disparate as property tax liens,17 involuntary mechanic’s liens,18 terminations of parking licenses,19 and waivers of potential legal actions.20

An extreme example of the nonintuitive nature of the transfer carveout is Blue Hills Office Park LLC v. J.P. Morgan Chase Bank.21 In that case, the borrower’s neighbor applied for a permit to build a garage.22 The borrower objected to the permit application but later withdrew its objection.23 Over a year later, the lender foreclosed and commenced an action to recover a $10.7 million deficiency personally from the borrower based on the transfer carveout.24 The court ruled that the borrower’s withdrawal of its objection to the neighboring development—despite not having any causal link to the actual default that led to the foreclosure, the $10.7 million deficiency, or indeed to any loss the lender incurred—constituted a violation of the carveout.25 Given cases like Blue Hills, and the seemingly endless ways to mix and match the definitions of “transfer” and “mortgaged property,” the practical risks to borrowers of unintentionally tripping the transfer carveout are almost inconceivable.

Expanding Personal Liability

A second major side effect of CMBS 2.0 is the requirement of new carveouts that did not exist in CMBS 1.0. Lenders, stung by the losses they suffered in the Great Recession—including those they believed were caused by the nefarious acts of borrowers—
invented carveouts to address matters for which the traditional remedy was nonrecourse default and foreclosure. For example, in response to borrowers’ intransigence and delay tactics during loan workouts, lenders now impose personal liability for failure to permit property inspections, deliver financial statements, appoint a new property manager, or cooperate in transferring licenses upon a foreclosure. In most of these cases, the purported bad act in question does not rise to the malefaneous level of traditional carveouts like fraud, misappropriation, or bankruptcy.

Further, in the new world of CMBS 2.0, lenders more often require certain catch-all carveouts (such as gross negligence and willful misconduct), which do not involve any specific bad acts or covenant breaches. This lack of specificity exposes borrowers to unpredictable and subjective risks, as opposed to traditional bad boy clauses that enumerate proscribed acts. In CMBS 1.0, these types of carveouts were either not required at all or routinely negotiated out by borrowers without much resistance.

One of the most controversial new carveouts imposes personal liability on a borrower if it interferes with or hinders a lender’s exercise of remedies. The reason for this carveout is clear, as during the recession borrowers often asserted lender liability claims in an effort to protect themselves from liability or foreclosure. Lenders in turn created an \textit{in terrorem} effect to deter such claims. For borrowers, this new carveout presents an obvious dilemma: abandon good-faith defenses to a lender’s foreclosure and lose the property, or fight to keep the property under the threat of springing personal liability.

For example, in \textit{Bank of America, N.A. v. Freed}, the borrower obtained a mortgage loan to finance its project, which later encountered financial difficulty.\textsuperscript{26} One of the springing full recourse carveouts in the loan documents required the borrower not to “contest, delay, or otherwise hinder” the lender’s exercise of remedies.\textsuperscript{27} The loan workout discussions became contentious, the lender filed a petition to appoint a receiver to wrest control of the project, and the borrower duly contested the appointment.\textsuperscript{28} The contest was short-lived, as just 30 days later the court appointed the receiver.\textsuperscript{29} Nevertheless, under a strict interpretation of the nonrecourse carveouts, the court rejected the borrower’s defenses and enforced full personal liability.\textsuperscript{30}

\textbf{Nonavailability of Equitable Defenses}

Given the courts’ strict interpretation of nonrecourse carveouts, often producing draconian and unanticipated results, borrowers have cried foul and looked to equitable defenses for protection. Among other things, borrowers have claimed that penalizing them with springing personal liability if the lender has suffered no actual harm is inequitable, unconscionable, and unenforceable. For example, the developer in \textit{Freed} argued that its “hindrance” of the lender’s appointment of a receiver for a mere 30 days did not warrant a judgment for $206 million.\textsuperscript{41} The office owner in \textit{Blue Hills} argued that its “transfer of property”—in actuality withdrawing its objection to a neighboring development—was not the type of bad boy conveyance that should merit a $10.7 million judgment.\textsuperscript{32} The apartment owner in \textit{Pineridge Associates, L.P. v. Ridgepine, LLC}, argued that its transfer of property—in actuality incurring a mechanic’s lien that was wiped out in foreclosure—did not warrant full personal liability under its loan.\textsuperscript{33} In all of these cases, the borrowers’ arguments were rebuffed by the courts.\textsuperscript{34}

Indeed, the vast majority of cases reflect an unwillingness to entertain, much less adopt, the equitable defenses of borrowers.\textsuperscript{35} In those cases, neither the immateriality of the breach, the disparity between the judgment amount and the loss, nor the absence of any loss at all has persuaded the courts otherwise. The opinion in \textit{CSFB 2001-CP-4 Princeton Park Corporate Center, LLC v. SB Rental I, LLC}—a case in which the borrower placed a $400,000 subordinate mortgage behind a $13 million senior loan and repaid the subordinate loan one year before the senior lender’s foreclosure—best sums up the common theme in the reasoning employed by many courts: “It matters not, as defendants argue, that they eventually cured the very breach that triggered their personal liability and that no harm accrued to plaintiff as a result thereof...defendants may not now escape the consequences of their bargain.”\textsuperscript{36} Undoubtedly, the \textit{SB Rental} decision leaves many nonrecourse borrowers wondering what happened to their fundamental bargain.

\textbf{What’s Next?}

CMBS debt surged in 2015 and, while the final numbers are still coming in, projected issuances totaled over $100 billion—more than in any other year in history except for the 2005–2007 peak.\textsuperscript{37} Because this surge coincides with rising commercial real estate values, there has been less distress in the markets and less litigation over nonrecourse carveouts. As history has taught, however, the surging market will not last forever, and the next black swan event could be just around the corner. When a market correction occurs, it will be impossible to predict what types of seemingly innocuous events will trigger springing personal liability.

Imagine making a deal with a neighbor that allows the use of the neighbor’s drinking fountain—would giving up that right constitute a transfer of property? How about objecting to that neighbor’s new paint color and then realizing you actually like neon green—by dropping your objection have you transferred property? And what if you ultimately dispute a lender’s foreclosure—did you improperly hinder the lender’s remedies? Or if you text the lender that you might not
make your next mortgage payment—did you admit your inability to pay debts?

While lenders (and at times borrowers themselves) may consider the above examples as absurd instances of lawyers being picky, case law suggests otherwise. As borrowers navigate their way through CMBS 2.0 and beyond, it would behoove them to meticulously review their existing loan documents, identify overbroad nonrecourse carve-outs that could trigger personal liability in unanticipated ways, and calibrate their behavior accordingly. In negotiating new nonrecourse loans, borrowers should ensure that any springing carveouts are narrowly drafted to encompass only intentional bad boy acts that are within the borrower’s control and will actually cause material harm to the lender’s collateral.

5 Other nonrecourse carveouts (such as misrepresentation and waste) have also been the subject of controversy, and difficult questions are raised when there is a change of control of the borrower and the new borrower subjects the old (unaffiliated) guarantor to personal liability.
7 Cherryland, 812 N.W. 2d at 815.
13 Id. at 1029-30.
14 Id. at 1025.
15 Id. at 1030.
16 See, e.g., BLACK’S LAW DICTIONARY (1999).
21 Id.
22 Id. at 370.
23 Id.
24 Id. at 371, 377.
25 Id. at 378-79.
27 Id. at *3.
28 Id. at *4-9.
29 Id. at *24-25.
30 Id. at *32-34.
31 Id. at *24-34.
34 Blue Hills, 477 F. Supp. 2d at 381; Freed, 983 N.E. 2d at *32-34; Pineridge, 337 S.W. 3d at 466-68.
35 While the vast majority of courts have rejected borrowers’ equitable defenses, other courts have taken a more balanced approach. See, e.g., CP III Rincon Towers, Inc. v. Cohen, 13 F. Supp. 3d 307 (S.D. N.Y. 2014); ING Real Estate Fin. (USA) LLC v. Park Ave. Hotel Acquisition LLC, 907 N.Y.S. 2d 437 (N.Y. Sup. Ct. 2010).

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MANY WEALTHY NON-AMERICANS see U.S. real estate as an attractive and secure investment opportunity and a safe vehicle by which they may expatriate cash from their home countries. Foreign investment in U.S. real estate reached $54 billion for the year ending March 2015.¹ Not surprisingly, the Golden State has topped the charts in market share, second only to Florida.² The majority of these sales are for single-family residences intended to be used as vacation homes or investment property.³ Sometimes foreign buyers acquire a home for their U.S. college-bound children. Whatever the reason for purchasing a home in California, foreign investors typically have a number of competing objectives. A common one is privacy. Since title to real estate in the United States is usually public record, wealthy foreign investors, particularly those that are public figures, are rightfully concerned about the public availability of the locations of their personal residences. As a corollary to this concern, many foreign investors do not want to file income tax returns in their individual names. Lawsuits are another common fear of foreign investors. While liability exposure for the ownership of a personal residence is arguably less than for a property that is being rented to unrelated third parties, foreign buyers often have concerns about America’s notoriously litigious society. Finally, foreign investors want to minimize income and estate taxes on their real estate investment. What many investors neglect to consider when investing in California is property tax, which can be significant, and the property tax impact of subsequent transfers of real property to their children by gift or inheritance.

When advising foreign purchasers of U.S. real estate, it is advisable to mention that under the U.S. tax system, U.S. residents are taxed on all the income they earn, whether it was earned in the United States or abroad. Most other developed countries employ a territorial tax system, which does not tax income from a foreign source. Many foreign investors are shocked to hear that their visits to the United States could cause them to become U.S. residents for tax purposes, subjecting them to U.S. tax on their worldwide income. A foreign individual is treated as a U.S. tax resident if either 1) the lawful permanent resident test or 2) substantial presence test is met.⁴ Under the lawful permanent resident test, those who hold green cards owe the U.S. tax on their worldwide income. Under the substantial presence test, foreign individuals are treated as U.S. tax residents if they are physically present in the U.S. for 1) at least 31 days in the current year, and 2) 183 days or more in the current and previous two calendar years, with a weighting formula used for the previous two calendar years.⁵ In order to avoid passing the substantial presence test and to maintain status as non-resident aliens (NRAs), foreign individuals must keep track of the time they spend here, especially if they are getting close to the 183-day threshold. There are some noteworthy exceptions under the substantial presence test, including time spent by foreign students, business visitors, professional athletes, and others.

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ships or LLCs holding real property are treated as U.S. situs assets is not entirely clear under current IRS guidance. The large exemption from estate tax for U.S. residents is unavailable for nonresidents; their exemption is only $60,000.11 California property tax is based on the fair market value of the property at the time of purchase.12 The tax rate is 1 percent annually plus any special or direct assessments, which vary from city to city. The fair market base value of a property is adjusted for inflation but only up to 2 percent per year. Thus, once real property is acquired, the property tax increases are relatively modest. Attorneys should advise foreign purchasers that their property taxes may be significantly higher than those of the current owners of a property. This cost needs to be taken into account when evaluating the investment.

The possible dramatic tax increase resulting from a change in ownership of real property includes transfers by gift or inheritance. A transfer of real property to a spouse, however, does not result in a reassessment of real property.13 In addition, a transfer of a primary residence to a child on death does not result in a reassessment, and transfers of up to $1 million of other than a primary residence is also excluded from reassessment.14 With respect to transfers of interests in entities that own California real property, if a person obtains more than 50 percent of the voting stock of a corporation or more than 50 percent of the total interest in partnership or LLC capital and profits, the transfer constitutes a change of ownership of the real property owned by that corporation or partnership.15 However, transfers of interests in entities that result in a spouse’s obtaining a greater than 50 percent interest do not result in a change of ownership.16

Structuring Alternatives

There are a number of ways to hold title to the real property to address these issues. No one solution meets all objectives, and thus the pros and cons of each structure need to be weighed in light of the foreign investor’s concerns.

The simplest and most straightforward structure is direct investment by the individual. The key advantage of direct ownership is the favorable long-term federal capital gain rate (currently at a maximum of 20 percent17) on the sale of the property if it is held for over a year. California, however, does not have a preferential capital gain rate, and the gain would be taxed at a current maximum rate of 13.3 percent. Direct investment also leaves open the possibility of being able to utilize the exemption for gain on the sale of a principal residence ($250,000 for singles and $500,000 for couples).18 If a person has more than one residence, determination of which residence is the principal one is made by an analysis of facts and circumstances. Ordinarily, the property that the taxpayer uses the majority of the time is treated as the principal residence.19 This creates a tension between obtaining principal residence treatment for a U.S. home and foreign quotas, and 3 1/3 percent for California purposes.8 A real property interest in the United States includes not only a direct interest in real property but also interests in certain corporations that own real property, known as U.S. real property holding corporations.7 The FIRPTA tax is enforced through a withholding mechanism in which buyers are required to withhold 10 percent of the gross proceeds from the sale of a U.S. real property interest for federal purposes, and 3 1/3 percent for California purposes.8 Since the withholding tax is on the total proceeds from the sale and not just the gain on sale, the amount of withholding may far exceed the NRA’s U.S. federal and California state tax liability. The withheld tax can be applied against the actual tax liability on the NRAs income tax return, and the NRA can obtain a refund if there was overwithholding.

The estate tax is only imposed on an NRA’s U.S. situs assets.9 U.S. real estate and stock in a U.S. corporation are treated as U.S. situs assets, while stock in a foreign corporation is not, even when the corporation’s sole asset is U.S. real property or all the stock of a U.S. corporation whose sole asset is U.S. real property.10 Whether interest in partnerships or LLCs holding real property are

The Rental Predicament

When a shareholder uses corporate property for personal purposes, the fair rental value of the property is includible in income as a constructive dividend to the extent of the earnings and profits of the corporation.1 In the context of a U.S. corporation holding real property, the question is whether the foreign individual shareholder should pay rent to the U.S. corporation for the shareholder’s free use of the property.

In a relatively recent case, G.D Parker Inc. v. Commissioner,2 the Tax Court held that a foreign individual’s free use of residential real property held by a U.S. corporation was a constructive dividend to its foreign parent corporation and ultimately to the foreign individual shareholder at the top of the structure. The result was that the U.S. corporation was liable for a 30 percent withholding tax on the constructive dividend to the foreign corporation. The Tax Court also denied expenses associated with the property on the grounds that the acquisition and maintenance of the property were primarily motivated by personal rather than profit-motivated purposes.

While the idea of a constructive dividend may seem alarming, such a distribution is not taxable as a dividend if the corporation has no earnings and profits. For example, a U.S. corporation that owns a single residential property that is not rented to third parties and has no other income or assets should not have any earnings and profits. Whether free use of corporate property by a shareholder could result in deemed rental income to a corporation that would generate earnings and profits, however, is a question that remains unanswered.

In the case of a U.S. corporation with no earnings and profits, a constructive distribution does not result in a taxable dividend to the foreign parent corporation. The distribution is first treated as a return of capital and, after basis is exhausted, capital gain. Where the shareholder is only using the real property occasionally, it would likely take many years before basis is exhausted as the deemed distributions would be small.

In light of G.D Parker and the risk of imputed rent, rental agreements at fair value should be considered when a U.S. corporation owns real property that the ultimate foreign shareholders are using primarily for personal purposes. The rental income can be offset by maintenance, depreciation, insurance, and other expenses so that there is no income tax liability resulting from the deemed rental payments, and potentially even losses that could be used in the future. In any event, the foreign shareholders would have to fund the property expenses in some manner, whether by capital contribution or loan to the U.S. corporation.

If actual rental payments are made to the U.S. corporation, questions of local business tax must be evaluated. Many cities in California impose taxes and registration requirements on doing business in their city. Rental real estate is a business activity subject to tax in many cities. Each city has its own tax rates and municipal code, so the rules of the particular city where the real property is located must be reviewed to determine whether and how much business tax might be owed on rental payments to the U.S. corporation. Notably, it is unwise to claim that no city business tax is owed because the activity of renting to the ultimate sole shareholder is not a business activity. Such a contention would undermine the position that maintenance, depreciation, insurance and other expenses of owning the residential property is a business expense for income tax purposes.—V.H.

1 Ireland v. United States, 621 F. 2d 731 (5th Cir. 1980).
2 G.D Parker Inc. v. Comm’n, T.C.M. 2012-277.
MCLE Test No. 253

The Los Angeles County Bar Association certifies that this activity has been approved for Minimum Continuing Legal Education credit by the State Bar of California in the amount of 1 hour.

1. U.S. residents are taxed only on income they earn in the United States.
   True.
   False.

2. Green card holders are U.S. tax residents.
   True.
   False.

3. It is possible to be treated as a U.S. tax resident by being physically present in the United States.
   True.
   False.

4. Withholding under the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) is 10 percent of the gain on the sale of a U.S. real property interest.
   True.
   False.

5. There is no estate tax imposed on nonresident aliens.
   True.
   False.

6. A transfer of real property to a spouse does not result in a reassessment of real property for California property tax purposes.
   True.
   False.

7. California real property held directly by a nonresident alien is subject to the U.S. estate tax.
   True.
   False.

8. A California LLC that is treated as a disregarded entity for federal tax purposes does not have to pay the $800 minimum tax on LLCs in California.
   True.
   False.

9. The parent-child exclusion from property tax change in ownership is not available for transfers of interests in LLCs disregarded for income tax purposes.
   True.
   False.

10. The interspousal exclusion from property tax change in ownership is not available for transfers of entity interests.
    True.
    False.

11. Stock in a foreign corporation is not a U.S. situs asset for purposes of the U.S. estate tax.
    True.
    False.

12. FIRPTA withholding does not apply to any sale of stock of a U.S. corporation.
    True.
    False.

13. The estate tax applies to the stock in a foreign corporation that is owned by a nonresident alien (NRA) if the foreign corporation owns U.S. real property.
    True.
    False.

14. Married couples can elect to treat an LLC as a disregarded entity for federal income tax purposes.
    True.
    False.

15. California real estate owned by a foreign individual directly is not subject to the estate tax.
    True.
    False.

16. California does not impose a withholding tax on the sale of California real property by an NRA.
    True.
    False.

17. Dividends from a U.S. corporation to a foreign corporation are generally subject to a 30 percent withholding tax.
    True.
    False.

18. California property tax is based on the fair market value of the real property at the time of purchase.
    True.
    False.

19. NRAs are eligible for preferential long-term federal capital gain rates on the sale of U.S. real estate.
    True.
    False.

20. NRAs are not subject to federal income tax on the sale of U.S. real estate.
    True.
    False.
while not spending so much time in it that the resident is treated as a U.S. tax resident. There will be FIRPTA withholding on the gross proceeds from the sale.

The main drawback of direct investment is that if the foreign owner dies while holding the real property, the property will be subject to the U.S. estate tax, which has a current maximum rate of 40 percent. For a young buyer with a relatively short investment time frame, the estate tax may be of little concern. For those who are older and wiser, a structure involving a foreign corporation should be considered. An intermediate solution for the young and invincible is to obtain life insurance for an amount equal to 40 percent of the net equity of the real estate value. Under California tax law, a transfer of a primary residence to a spouse or to a child on death does not result in a reassessment of the property.20

Another disadvantage of direct investment is lack of privacy. The name of the individual NRA owner is a matter of public record, the NRA is required to file U.S. tax returns in her or his name on the sale of the property, and there is no liability protection.

A solution to the privacy and liability concerns is taking title in the name of a single-member LLC—which is disregarded for federal and California income tax purposes. Married couples owning the LLC as community property (even under the laws of a foreign country) can elect to treat the LLC as having only one owner, with the result that it is a disregarded entity.21 Although the income tax treatment is the same as if the NRA directly owned the property, California imposes an $800 annual minimum tax on LLCs that are disregarded entities, plus a gross receipts tax. The gross receipts tax, which would apply in the year of sale to the gross sales proceeds, ranges from $900 if the total gross receipts are between $250,000 and $500,000 and up to $11,790 if the gross receipts exceed $5 million.

Upon the death of the NRA investor, the LLC membership interests are subject to the estate tax. Addition, the parent-child exclusion from property tax change in ownership is not available for transfers of entity interests, although the interspousal exclusion is available.22 However, unless a child of the NRA inherits more than 50 percent of the total interest in LLC capital and profits, the transfer of the LLC interests does not constitute a change in ownership for property tax purposes.23 Thus, if an NRA dies with only one child as an heir, the real property held in the LLC is reassessed at current fair market value. On the other hand, real property held in an LLC owned by an NRA who dies with two children as equal heirs does not undergo a reassessment, as no child would obtain more than a 50 percent interest in the LLC.

The main benefit of the LLC structure compared to direct ownership is limited liability protection. As compared to a corporation, the remedies for a creditor’s claims against an LLC are more limited. LLCs do not require compliance with corporate formalities such as shareholder meetings and keeping minutes in order to maintain protection against creditors. LLCs also offer increased privacy, as the name of the LLC, not the person, is listed in the public records as the owner of the home. However, the California LLC 12 Statement of Information lists the names of the managers or members of the LLC, and this form can be obtained by anyone from the California Secretary of State. Moreover, the tax filing requirement in the name of the individual NRA remains.

A foreign corporation structure is commonly recommended to hold U.S. real property, as stock in a foreign corporation is not subject to the U.S. estate tax. This could be structured either as direct ownership by the foreign corporation or ownership of the real estate by a U.S. corporation that is held by a foreign corporation. In either case, the ultimate owner would be the NRA. While avoidance of estate tax is a clear advantage to this structure, the income tax result is not ideal. Corporations, domestic or foreign, are not eligible for long-term capital gain rates. Thus, gain on sale of the real property in either case would be subject to tax at a maximum rate of 35 percent rather than the long-term capital gain rate of 20 percent. In addition, California imposes an $800 annual minimum tax on corporations organized in or doing business in California, plus a net income tax of 8.84 percent.

Another consideration for a corporate structure in which a foreign corporation owns the U.S. corporation that owns the property, in addition to the income tax at the U.S. corporate level, a dividend distribution from the U.S. corporation to the foreign corporation would be subject to a 30 percent withholding tax.24 In other words, this structure creates a double tax. However, if there is a liquidating distribution (e.g., the real property is sold and the U.S. corporation is liquidated) the 30 percent withholding tax does not apply. The direct foreign corporation ownership structure also has this double layer of tax as a result of the imposition of the branch profits tax. It is possible to avoid the branch profits tax, however, by terminating the foreign corporation’s U.S. business. From a California property tax perspective, the transfer of the shares of stock to a spouse on death would not result in a property tax reassessment. However, a transfer of the shares to another heir would result in a property tax reassessment if an heir acquired more than 50 percent of the foreign corporation.

Like an LLC, a corporate structure provides privacy in that the corporation’s name is listed as the owner of the real property on the public records. Nonetheless, Form 1120-F, the U.S. income tax return of a foreign corporation, requires listing shareholders who own 50 percent or more of the corporation. Therefore, NRA majority shareholders of a foreign corporation owning real estate in the United States are required to put their names on the tax returns, although the NRA is not required to obtain a taxpayer identification number.

In structuring an NRA’s purchase of a home in California, one has to keep the California-specific income and property tax implications in mind while also balancing the federal income and estate tax consequences, privacy concerns, and liability protection issues. Even if everyone wants to live to California, not every investment structure works for everyone.
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AS JOHN DONNE FAMOUSLY WROTE, “No man is an island...every man is a piece of the continent, a part of the main.”¹ Millions of Los Angeles County property owners can relate to Donne’s meditation because, with rare exception, each has one or more next-door neighbors. Given enough time, property owners will likely experience some legal issue over their property or that of a neighbor. These typically mundane issues are usually resolved amicably because the amount at stake is relatively de minimis when compared with the cost of retaining counsel and litigating or arbitrating the dispute. Nevertheless, disputes arise when there is sufficient antipathy between neighbors or the legal and financial consequences are so great that they can only be resolved through some form of legal proceeding. These disputes often relate to the location of land boundaries; structural encroachments; easements; fences and walls between properties; trees, hedges, and roots near boundaries; rights to sunlight and scenic views; noise and other nuisances; and attractive nuisances or dangerous conditions. When these disputes arise, it is advisable to grasp California civil law pertaining to property rights vis-à-vis one’s neighbors, specifically concerning single-family, detached residences over which no homeowners association governs.

Disputes concerning the coherence of recorded lot lines are becoming rare in established communities. When such coherence is lacking, litigation may be inevitable if the parties cannot sort out the problem through quitclaim deeds or a lot line adjustment.² Statutes guide California’s courts and parties concerning how to resolve ambiguities and mistakes in deeds.³ In the case of single-family, detached residential parcels, the locations of lot lines are usually determined by reference to the recorded subdivision map under which the lots were created.⁴

California law provides some clear answers on such sources of conflict between neighbors as encroachments, lot lines, fences, and trees

by ANDREW R. HENDERSON

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When coherent lines, arcs, angles, distances, etc., are recorded in a subdivision map or by metes and bounds or other narrative description, the recorded descriptions are almost always determinative—except when the doctrine of agreed boundary or adverse possession might apply. The need remains, however, to translate information from county records onto the terrain, which usually requires a professional land surveyor. Long ago, surveying was error-prone, especially in wooded or uneven terrain. Advances in modern surveying, however, have significantly lessened concerns about the reliability of surveys. Any landowner undertaking an improvement near the edge of neighboring property, even constructing a modest fence, is advised to hire a professional surveyor to stake the lot line if its location is uncertain, because the encroached-upon neighbor may seek to correct any mistake. The next-door neighbor also should monitor the activity because the law could deprive him or her indefinitely of the use of the land on which an encroachment sits. Moreover, over time, recollections and evidence about an improvement’s origin, parol agreements, friendly permission, etc., all tend to fade or get lost. Principals and witnesses may pass or move away. In short, laxity concerning the true location of boundaries invites later confusion.

Lot lines described in recorded documents are not always dispositive. A lot line can effectively be relocated based on the ripening of a parol agreement made between uncertain neighbors. Under the agreed boundary doctrine, recorded lot lines will be relocated by operation of law when there is proof of 1) mutual uncertainty between neighbors concerning the true boundary line, 2) an express or implied agreement between the neighbors to accept a particular line as the boundary, and 3) either acceptance and acquiescence in the new line for the prescription period (five years) or, if earlier, when an action is taken in reliance of the agreement that would result in substantial loss if the recorded boundary were reinstated. Thus, even when the facts are disputed, if a preponderance of the evidence reflects 1) mutual, coincidental confusion between neighbors, and 2) a long-standing or consequential resolution thereof, recorded lot lines can be ignored and permanently relocated.

Importantly, a buyer who purchases a parcel that is already diminished by an agreed boundary can later suffer a surprising shortage of land even if there were no notice to the buyer about an earlier agreement. Therefore, real estate purchasers should be aware that the agreed boundary doctrine is an exception to the rule giving legal effect to a land description contained in a recorded deed, and they should look for any indications of such an agreement. The doctrine might possibly be raised when there is an encroachment over, or perhaps a fence placed some distance away from, a recorded lot line.

**Encroachments**

Encroachments happen in urban, suburban, and rural settings. The best advice about encroachments is simple. Strictly avoid building any improvement on, over, or under someone else’s land—other than perhaps a properly noticed division wall exactly straddling the property line—unless the record owner gives express written permission to do so. Doing otherwise can give rise to a costly dispute over whether the encroachment was hostile, permissive, accidental, or perhaps following an agreed boundary.

When the record owner gives neither express nor implied permission, an encroachment constitutes a trespass or nuisance, subject to a timely suit to quiet title (which can include a prayer for the recovery of possession or injunctive relief) that also may include damages. In the past, many courts, when adjudicating structural encroachments, applied the same three-year limitations period that applies to fleeting trespasses. More recently, however, the courts have carefully considered the interplay between the trespass statute and the adverse possession statute. They now instead apply the five-year statute of limitations and other law applicable to disputes involving title to land—adverse possession. Authority exists for the proposition that a structural encroachment that juts into a neighbor’s airspace only—not touching the encroached-upon land at or below grade—constitutes an abatable continuing nuisance, and no statute of limitation should bar a lawful suit. A special rule applies to a latent encroachment that is located entirely below grade. In this case, the encroached-upon owner enjoys the right to self-help (i.e., removing the encroachment at the encroacher’s expense without resorting to litigation) after giving reasonable notice and an opportunity to remove it. In all other cases involving structural encroachments, self-help is unavailable and legally actionable. Thus, the record owner is advised to sue to redress the encroachment. California law defines when and under what circumstances—given time or other factors—an encroachment can ripen into either a prescriptive taking of the land or, more likely, qualify for the imposition of an equitable easement to continue to occupy the land. Generally, one can appropriate a legal interest in another’s land (either ownership or an easement) by openly, notoriously, continuously and without interruption, and with hostility possessing or using it, under claim of right, for five years. To gain actual ownership of the land (rather than lasting use), the adverse possessor must pay all property taxes levied on the land during the five-year prescription period.

If an unwelcome encroachment has not yet been in place for five years, a court may nevertheless award an equitable easement for the encroachment’s continuation when the balance of relative harm between the parties warrants this relief. A court will typically do so only if the party seeking to maintain the encroachment was neither knowing and willful nor sufficiently negligent in causing the encroachment. Therefore, one who intentionally encroaches should never enjoy an equitable easement and, instead, needs to satisfy all elements of adverse possession. When courts grant equitable easements, they usually require the encroacher to compensate the record owner for the ongoing use of the land, and pay damages if proven. One who takes by prescription usually pays nothing for the acquired interest (other than the property taxes during the prescription period if ownership is taken).

Three factors play relatively significant roles in deciding if an encroachment has ripened into a prescriptive or equitable right and, if so, what kind: 1) exclusive use of the affected land, 2) payment of property taxes, and 3) adversity versus permission. First, courts focus on whether an encroachment prevents the record property owner from using the land encroached upon—such as an encroaching building or wall enclosing the encroaching party’s yard. Courts hold that an exclusive easement—one that excludes the encroacher generally should not obtain a prescriptive easement for the adverse, exclusive use of a portion of the neighbor’s land because it would be tantamount to actively appropriating ownership without paying property taxes levied. In addition, courts have opined that a prescriptive easement should never be found concerning a garden-variety boundary encroachment without defining what one is. Therefore, to the extent that a more-or-less typical exclusive encroachment might result in an easement, it should be only in equity.

Second, in order for an adverse possessor to gain a fee interest in land, one must pay the property taxes levied on the land throughout the prescription period. Few who build an encroachment on a neighbor’s property will actually pay property taxes levied on the affected land, and it seems unlikely that someone could do so unnoticed. Practitioners should be aware, however, that courts...
have recognized a “natural inference” that local officials levy taxes on the underlying land when they levy taxes on structures. Therefore, when such a factual inference might be drawn, merely paying the property taxes levied on the encroaching structure or other improvement can constitute sufficient evidence of paying property taxes levied on the land, satisfying the statutory element.

Countering the inference requires marshalling evidence of the local taxing authority’s actual, contrary property assessment practices—i.e., one should prove that the encroachment resulted in no lessening of the property tax levied on the record owner’s land.

Third, adversity is one of the most contested elements of adverse possession. This element can be arcane and does not require an intention to appropriate land that one knows to be a neighbor’s land. Instead, an encroacher’s innocent mistake or inadvertence about whose land is being occupied is construed as adverse, hostile and under a claim of right unless the court finds that the encroacher knew that there was a potential of encroachment and intended to disclaim ownership if an encroachment upon record title were in fact the case.

Generally, hostility and adversity are not present; therefore, the requisite elements are not satisfied if the possession or use of the land is maintained with the record owner’s express or implied permission—for example, by license. Importantly, each element of appropriation by adversity must be proven by clear and convincing evidence. However, each element of adverse possession or use is ultimately a question of fact and, thus, is subject to both dispute and ultimate factual findings that are hardly appealable under the applicable substantial evidence test. Therefore, if one wishes to permit an encroachment or use only temporarily—neither permanently nor for the encroachment’s natural useful life—one should provide permission in a writing that clearly sets forth any and all qualifications, and preserve, or, ideally, record, the evidence.

If the permission given by a record owner is unclear or unqualified, the owner may later be barred from ejecting an encroachment, terminating a use, garnering damages, or quieting title. Specifically, an unqualified license to build an encroaching improvement can become irrevocable for the natural life of the improvement thus constituting an irrevocable license. In short, one’s permission should negate a future claim of adversity (and thus prescription), but it can also invite claims of estoppel or irrevocability or both. Therefore, clarity and proof concerning the exact extent of one’s permission are advised.

Easements
An easement is defined as a right to use or affect the land of another for a specific purpose, which is less than an ownership or possessory (e.g., a tenant’s) right. An easement typically involves the right to use a neighbor’s driveway or land for ingress and egress, or perhaps for parking or to turn vehicles around. In addition, with a landowner’s permission, a person may acquire an easement to construct and use a permanent structure, such as a garage, on another’s land.

Easements may be established by a variety of means, including agreement, prescription, necessity, implication, condemnation, estoppel, and or by equitable considerations (out of a sense of reasonableness and balance). Easements by necessity are rare, and arise, for example, when land is subdivided so that one parcel is entirely surrounded and an easement is necessary for access. An easement by implication arises when the actions of one or more parties conveys an intention to burden land with such an easement, such as when a subdivider builds, or when neighbors jointly build, either a party wall (then or thereafter incorporated into dependent structures) or a division wall straddling a property line. Most easements seemingly arise by agreement, by prescription, by estoppel, or by equity. In each instance, evidence reflecting the record owner’s permission and the parties’ foreknowledge and intentions is crucial. Permission concerning the temporary use of one’s land (e.g., a revocable license) should be carefully memorialized in terms of any and all qualifications, lest the facts are called into dispute, and estoppel or irrevocability might adhere. Once an easement is found to exist, it will usually continue until it is abandoned, terminated by agreement or prescription, or if ownership of both the dominant and servient tenements becomes unified.

Fences
Specifically concerning fences and division walls, Robert Frost once penned, “Good fences make good neighbors.” However, fences are not all beloved, and they can become sources of neighbors’ conflict. In theory, California law compels abutting neighbors to cooperate concerning the construction, maintenance, and replacement of division walls between properties. Specifically, Civil Code Section 841 provides 1) an obligation for neighbors to cooperate concerning such division walls or fences (their construction, maintenance, and replacement), 2) a presumption that the neighbors are mutually benefitted and should equitably share the costs thereof, 3) the factors that could warrant an equitable departure from the equal sharing of costs, and 4) prescribed steps for obtaining one’s neighbor’s participation and contribution towards the costs of such an improvement.

In practice, however, a number of factors weigh against relying on the division wall statute in typical residential situations. First, the litigation costs associated with enforcing one’s statutory rights would likely exceed the total cost of most division walls. Second, one neighbor will typically want to dictate the aesthetics and cost of a wall or fence, warranting a departure from the statutory presumption about the mutuality of benefits and
nearby land. Civil Code Section 832 imposes maintaining the lateral support of adjacent and receiving no objection about the proper division fence on the actual property line and recover half the cost after given proper notice. Section 841 implies that a property owner able to invoke the statute nor otherwise debate a mutually agreed-upon light-and-view easement or private rights and obligations that a homeowners association might enforce. An example of a local view ordinance is that of the city of Rancho Palos Verdes, which protects neighbors’ views from growing trees and foliage.

Trees, Light, and Views
Concerning trees, John Muir, California’s famous naturalist, once wrote that he never saw a discontented tree. Human beings, however, sometimes experience discontent concerning their neighbors’ trees. In many cases, their discontent will persist, because California law is generally protective of trees.

One should never go onto one’s neighbor’s land and trim or cut any tree or bush growing there. Not only is it a compensable trespass; but it also can result in an award of double or treble, or both actual and punitive, damages—depending on whether the act is negligent or willful, plus a plaintiff’s attorney’s fees. One may trim the branches that grow from a neighbor’s land over one’s own land, however, and keep clear the airspace over one’s land to the property line. A similar right does not apply to cutting roots that grow across the property line into one’s land. One may cut roots back to one’s property line only if it is reasonable under the circumstances, for example, if needed to prevent property damage.

While the law generally protects trees, planting one in one’s own yard too close to the property line is not a particularly civil act in the layman’s sense. As noted, trees or a hedge planted near a property line may constitute a spite fence. The cross-boundary growth of roots can cause problems, and leaves, as well as perhaps other tree parts, will likely fall across the boundaries.

Perhaps worse than locating a tree too close to a property line is locating a tree exactly on a property line. Once it becomes established, such a tree is called a “line tree” and is owned in common by the two adjoining neighbors. Neither neighbor may harm a line tree without the permission of the other unless willing to pay to the other multiplied damages and attorney’s fees. Concerning light and views, California law has not provided landowners with any common law right to enjoy a view or ongoing sunlight. Only a few such rights now exist statutorily. One such statute—the Solar Shade Control Act—helps to ensure that homeown-ers can use solar energy, and effectively provides a limited easement vis-à-vis neighbors to collect sunlight on “solar collectors” that are located on one’s property. Another set of statutes—the Solar Rights Act—limits local governments’ power to restrict the placement of unsightly solar collectors on rooftops, and requires local governments to expedite applications for permits related to the use of solar energy.

Although state law does not confer a right to enjoy one’s scenic views, some localities have enacted ordinances that specifically protect views. These ordinances grant rights similar to those arising from a private commitment such as an agreed-upon light-and-view easement or private rights and obligations that a homeowners association might enforce. An example of a local view ordinance is that of the city of Rancho Palos Verdes, which protects neighbors’ views from growing trees and foliage.

Nuisances
Concerning noise and similar nuisances, “Nothing makes you more tolerant of a neighbor’s noisy party than being there.” Neighbors must often tolerate impositions like a barking dog or very noisy party next door. Concerning more serious matters (and setting aside consideration of local ordinances), the law provides that landowners and tenants have a legal right to the “quiet enjoyment and use” of their property, a violation which can give rise to a cause of action for a private nuisance.

A private nuisance is defined as a substantial and unreasonable interference with the quiet enjoyment and use of property. Cases tend to rise or fall based on proof of the degree of substantiability of the complaint about interference with the right to quiet use. The primary question—generally one for a jury—is whether the interference with use and enjoyment of land would be offensive or inconvenient to the normal person.

An “attractive nuisance” is a term of art connoting a dangerous property condition that attracts children in particular. Prior to 1970, California law recognized the attractive nuisance doctrine and provided that tres-
passing children—unlike trespassing adults at the time—could sue a negligent property owner for harm caused by dangerous property conditions and prevail by proving a lack of understanding of the risk (among the other elements).74

In 1970, California abolished the attractive nuisance doctrine because evolving case law held that trespassers and invitees, regardless of age, could sue for harm caused by negligently maintained dangerous conditions on one’s premises.75 Under current law, “one is responsible...for an injury occasioned to another by his or her want of ordinary care or skill in the management of his or her property or person, except so far as the latter has, willfully or by want of ordinary care, brought the injury upon himself or herself.”76 Therefore, one must manage one’s real property as a reasonable person would in light of the probability of risk to others.77 The nature of a given risk will factor into the degree of care owed, for example, having a swimming pool or a vicious guard dog will inform one’s duty of care to protect others.78

Thus, California law provides many answers concerning the mundane conflicts that may arise between neighbors. When counseling a client about any neighborly conflict, careful circumspection toward the law is warranted. Moreover, take note that neighbors’ conflicts are often more about emotions and egos than the law and objective facts. In the final analysis, the best advice is: Use common sense, seek reasonable accommodation, and try hard to be polite and friendly.
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Videoconferencing Can Help Our Courts and Improve Access to Justice

**MOST CALIFORNIANS** come into contact with the legal system only a few times in their lives. Typically, their cases are not high-profile, involving traffic tickets, family law matters, and small claims court. Despite the best efforts of attorneys and judges, justice still comes at a high price for many. People have to take time off from work (losing much-needed wages), pay for childcare, travel to the courthouse, and wait in long lines. To make justice more accessible to Californians, it is time to accelerate the use of streaming video technology. This technology can serve as a practical alternative for ordinary people with routine court matters who currently have to spend many hours to obtain a five-minute court appearance.

While courts grapple with severe budget cuts, one cost-cutting solution is to implement video technology for ordinary court appearances. When scheduling a face-to-face appearance with a judge for straightforward issues such as contesting a speeding ticket, attending a family law hearing, or disputing a small claims court issue, this technology can save time, money, and energy. No longer will Californians need to take a day off work to wait for their matters to be called.

With courts having been deprived of more than a billion dollars in funding in a few years, videoconferencing could be a game changer. Courts can see less overcrowding, particularly in criminal courts, where some hearings last less than five minutes. There will no longer be a need for courtrooms packed with people waiting to be heard. Rather, the judge can have a queue of matters ready to call, and conference with each defendant in turn. Videoconferencing would be beneficial over court calls and drastically reduce courtroom costs.

This technology can be implemented in other judicial matters in which parties typically appear pro per. Parents living in different jurisdictions can use video streaming for routine appearances in family law matters. Recently, in a high-profile custody case that involves actress Kelly Rutherford, her ex-husband Daniel Giersch, who lives in Monaco, appeared by video streaming during a custody hearing in New York. This technology is not just for the rich and famous. Working-class people should also be able to use it.

Employers would also benefit from video streaming for court appearances. Since employees would no longer need to take days off work to appear in court, it could take only an hour or two waiting for their matters to finish, lessening the impact to productivity. Employees could use videoconference systems already in place at their workplace to make their court appearances and then return to work.

There are some matters to address. For example, during the highly publicized criminal trial of George Zimmerman in 2013, witnesses using Skype were interrupted by phone calls made into the Skype account being used. This made it hard to hear over the rings of the incoming calls and caused a delay in the proceedings. However, there is an easy fix—the individual making the call could change the settings so that only parties on the individual’s contact lists could make video calls and then create a contact list with only the witness on the list. With practice, use of easily accessible videoconferencing tools such as Skype can improve.

Videoconferencing is already being used elsewhere. In Singapore, attorney use of videoconferencing is common. There are designated Skype contacts for different chambers servicing different court hearings. Attorneys message their respective chambers when they are ready to proceed, state their name, law firm, and case number, and wait for the judge to initiate the video call. This works in a manner similar to CourtCall here in Los Angeles, which is currently used by many attorneys making appearances for matters that do not require a presence in chambers. The same can be accomplished for litigants appearing pro per, with the added benefit of being face-to-face with the judge. Recently, the Fresno County Superior Court, in collaboration with the cities of Coalinga and Mendota, began a trial with Remote Video Proceedings (RVP). The program allows those who were issued citations outside the Fresno-Clovis area, and who need to travel in excess of 15 miles to appear in traffic court in downtown Fresno, to appear via videoconference.

The Fresno program has been such a success that the Judicial Council of California has proposed an amendment to California Rules of Court Rule 4.220, which allows for RVP trial programs. The current rule, which is set to expire this month, authorizes trial courts to establish remote video pilot projects by local rule. The program is subject to the approval of the Judicial Council in cases involving traffic infractions. Essentially, the amendment would allow trial courts to conduct RVP in eligible traffic cases so long as the courts adopt a local rule permitting RVP, notify the Judicial Council, and comply with a semiannual reporting requirement. The passage of this amendment can only help strengthen the judicial system as a whole, while saving time and money for litigants, attorneys, employers, and the court.

Ultimately, what we need is a massive expansion of the use of video appearances for routine matters involving self-represented parties. These smaller matters are the bread and butter of our judicial system, and the better they work for ordinary Californians, the better our justice system is working for all of us.

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