Los Angeles lawyer Andrea C. Chang explains the role and powers of court-appointed real estate receivers page 22
Chapman University School of Law
2010 Law Review Symposium
Friday, January 29, 2010, 9:00 a.m. to 5:00 p.m.

DRUG WAR MADNESS:
Policies, Borders & Corruption

Panel 1: Current U.S. Drug Policy and Alternative Paradigms

Confirmed Panelists Include:
Hector Berrelleza: Agent, Drug Enforcement Agency
Hon. James P. Gray: Judge, Orange County Superior Court
Asa Hutchinson: Director of the U.S. Drug Enforcement Administration and first Under Secretary for Border & Transportation Security at the U.S.D.H.S
Alex Kreit: Assistant Professor of Law and Director of the Center for Law and Social Justice, Thomas Jefferson School of Law

Panel 2: Cross Border Flows: Drugs, People and Trade

Confirmed Panelists Include:
Jennifer Chacon: Professor of Law, U.C.I. School of Law
Ruben Garcia: Associate Professor of Law, California Western School of Law
Kevin Johnson: Dean and Mabie-Apallas Professor of Public Interest Law and Chicana/o Studies, U.C. Davis School of Law

Panel 3: Narcoterrorism, Organized Crime & Political Corruption

Confirmed Panelists Include:
Dr. Rachel Ehrenfeld: Director of the American Center for Democracy

Moderators include Orange County Superior Court Judge James Rogan and Chapman Assistant Professor of Law Ernesto Hernandez. Additional panelists and moderators will be announced.

Keynote Address by Michael Chertoff

Michael Chertoff was the second United States Secretary of Homeland Security under President George W. Bush and co-author of the USA Patriot Act. He previously served as a judge on the United States Court of Appeals, as a federal prosecutor, and as assistant United States Attorney General. Since leaving government service, Mr. Chertoff has worked as Senior “Of Counsel” at the Washington, D.C. law firm of Covington & Burling. He also co-founded the Chertoff Group, a risk management and security consulting company.

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Mr. Gleitman has practiced sophisticated estate planning for 26 years, specializing for more than 14 years in offshore asset protection planning. He has had and continues to receive many referrals from major law firms and the Big Four. He has submitted 52 estate planning issues to the IRS for private letter ruling requests; the IRS has granted him favorable rulings on all 52 requests. Twenty-three of those rulings were on sophisticated asset protection planning strategies.
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PRE-EMPLOYMENT | BACKGROUND INVESTIGATIONS | PROSPECTIVE CLIENT
At the entrance to the Stanley Mosk Courthouse in downtown Los Angeles stands a sculpture, created by Donal Hord, titled Justice. It features a female figure dressed in judicial robes who is holding a globe and a sword, with a scale balanced on her head. The work, which also displays an American eagle, packs a symbolic punch for all who walk through the courthouse doors. It suggests the universal power of the law to bring impartial justice. I am sure that many students carry in their minds a similarly dramatic and idealistic image of the law as they enter law school, ready to prepare themselves to do their part for truth, justice, and the American way.

But I think few practicing lawyers feel that their purpose is to further the search for truth or ensure that justice is done. An incident from early in my career is illustrative. I attended a mediation before a retired judge. The case involved an elderly woman with diabetes who claimed it was the defendants’ jackhammering, and not her advanced illness, that caused her to go blind. The case was probably without merit, but the defendants had made some mistakes, and a poor woman was blind.

The mediator spent most of the day working with the lead defendant in the room next door to me. The defendant wanted vindication and could not accept the reality of the situation. At one point they raised their voices loud enough so that I could hear through the wall. I heard the defendant yell, “You want justice and you came to the courts?”-—and the mediator yelled back incredulously, “You want justice and you came to the courts?”

One of my first mentors in the legal profession told me that people hire him to win for them. They want justice and will pay good money to win it for them. It is a common misunderstanding among those in the legal profession.

Sometimes, however, it all becomes clear what it means to be a lawyer. A friend who operates a small business recently came to me for advice. Her landlord was trying to raise her rent 20 percent. She was distraught, certain that this would sink her business. I studied her lease, pointed out the provisions that prevented the landlord from unilaterally imposing such a high increase, and explained how she could pressures him into a more reasonable compromise. She called me a few weeks later to say that she had worked out an agreement with the landlord to renew the lease with only a fractional increase in rent that she could easily handle. Her business was saved.

As soccer announcers so famously shout, stretching the word to use every last bit of air in their lungs, “Goal!”

For a lawyer, it does not matter if your client is a small business owner, a wrongfully accused murderer, a corporate titan, or a victim of a crime. When your advice gives others the strength and clarity to accomplish their goals, you find your purpose.
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Targeting ISPs in the Enforcement of Intellectual Property Rights

PROTECTING A BRAND from counterfeiters and copyists has been an uphill battle fought at flea markets, international borders, and on the Internet. A unique difficulty in fighting counterfeiters on the Internet is that the infringer, along with its factory and shipping department, is often overseas. This leaves brand holders scratching their heads as to how to stop the infringer’s fake products from entering the United States.

A recent case from the Northern District of California may provide a blueprint for brands to enforce their intellectual property rights online by targeting the Internet service provider that hosts the counterfeiter’s Web site rather than the counterfeiter itself. In Louis Vuitton Malletier, S.A. v. Akanoc Solutions, Inc.,1 a jury recently awarded Louis Vuitton $32.4 million against ISPs for contributory copyright and trademark infringement for their role in hosting Web sites that sold counterfeit products. In light of this holding, Web site operators must rethink how they will respond to infringement notices as they may be held liable for the actions of their counterfeiting customers.

Louis Vuitton was able to reach the ISPs because federal law protects against not only direct copyright and trademark infringement but also secondary infringement. As a threshold matter, establishing secondary liability for copyright or trademark infringement first requires proving an underlying direct infringement by a third party.2 To prove contributory copyright infringement, the brand holder must establish 1) knowledge of another’s infringement and 2) either material contribution to the infringement or inducement of the infringement.3 To prove contributory trademark infringement, the mark holder must prove that the defendant “(1) intentionally induced the primary infringer to infringe, or (2) continued to supply an infringing product to an infringer with knowledge that the infringer is mislabeling the particular product supplied.”4

Until the Louis Vuitton verdict, the path for brand holders to protect their rights against ISPs was less certain. In May 2008, the Southern District of New York granted summary judgment for eBay in a case in which jewelry manufacturer Tiffany attempted to enforce its trademark rights against eBay for hosting auctions for counterfeit Tiffany products.5 Unlike the Louis Vuitton case, eBay had been responsive when Tiffany provided actual notice of auctions of apparent counterfeit goods by quickly canceling the auctions. But Tiffany thought eBay should do more than react to Tiffany’s complaints. Tiffany wanted eBay to take preemptive actions and remove listings of Tiffany jewelry if eBay could reasonably anticipate that counterfeit goods might be sold on its Web site. Instead the court sided with eBay and held that the law does not weigh “whether eBay or Tiffany could more efficiently bear the burden of policing the eBay website.”5

The court determined that while the Internet offers new ways for sellers and buyers to connect beyond geographical limits and affords counterfeiters new opportunities to expand their reach, it is the burden of brand holders to police for infringement.

In Louis Vuitton, the brand holder had policed for infringements and provided numerous notices to the defendants to remove the offending sites. On the copyright claim, the ISPs unsuccessfully argued that despite the notices, they did not have knowledge of infringements because they did not verify whether an allegation by Louis Vuitton was well founded. Instead, the ISPs presumed all notices were well founded and issued their own takedown notices to their customers, the counterfeiters. The ISPs should have followed the requirements of the safe harbor provisions under the Digital Millennium Copyright Act (DMCA) and taken the extra step of disabling the allegedly offending sites. But the Louis Vuitton jury specifically determined that the ISPs failed to follow the DMCA requirements and could not take refuge under its safe harbor provision.

The ISPs also unsuccessfully argued that they did not materially contribute to infringing activity. However, A&M Records, Inc. v. Napster, Inc.6 holds that when “a computer system operator learns of specific infringing material available on his system and fails to purge such material from the system, the operator knows of and contributes to direct infringement.” Here it was the ISPs’ failure to purge infringing activity that led to the contributory infringement finding; merely providing takedown notices was deemed insufficient action to insulate the ISPs from liability.

Similarly, on the trademark claims, the court determined that the ISPs had the ability to control infringing uses of its services by terminating Web sites. The court likened an ISP to the flea market operator in Fonovisa v. Cherry Auction, Inc.,7 who was not permitted to remain “willfully blind” to the direct infringing activities of those whom the flea market operator allowed to use his premises.8 Further, the DMCA safe harbor does not insulate an ISP against claims of contributory trademark infringement.

The Louis Vuitton decision, along with Tiffany v. eBay, Inc., reinforce the idea that while the Internet is still a new frontier, the law is catching up. As a practical matter, ISPs must be vigilant about responding to takedown notices and properly follow the DMCA provisions. Promptly responding to takedown notices by disabling specific IP addresses to purge infringing activity from their networks may help avoid liability and high jury awards. Brand holders should continue to monitor infringements on the Web and, with some Internet savvy, identify the infringing sites’ ISPs and send notices of infringement with takedown demands. Brand holders should also familiarize themselves with DMCA takedown procedures and their limits, as there are penalties for filing false takedown notices.

Mark Kachner is an associate at Knobbe Martens Olson & Bear whose practice focuses on protecting IP rights and defending infringement claims involving patents, trademarks, copyrights, and trade secrets.

2 Perfect 10 v. Visa Int’l Serv. Assoc., 494 F. 3d 788, 795-807 (9th Cir. 2007).
3 Id. at 795.
7 Fonovisa v. Cherry Auction, Inc., 76 F. 3d 259, 264 (9th Cir. 1996).
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Resolving Remedy and Preemption Issues in Credit Reporting Cases

IN AN ECONOMY IN WHICH CONSUMERS INCREASINGLY RELY upon the accuracy of their credit reports to survive financially, laws that regulate credit bureaus and financial institutions and, in turn, protect consumers are becoming more prominent and essential. Despite industry efforts to attain the “maximum possible accuracy” mandated by the Fair Credit Reporting Act, credit reporting errors continue to plague consumers.\(^1\)

Inaccurate credit reporting can spell financial ruin. For example, the Fair Isaac Company, which licenses use of its FICO score to the credit bureaus, informs consumers that a single derogatory mark can deny a consumer credit on favorable terms—in spite of numerous other positive credit records.\(^2\)

Erroneous information on a personal credit report can affect more than just applying for credit cards or home loans. Pulling a credit report has become an expected and accepted part of a background check for applications for employment, public office, or any position of trust. Further, insurers sometimes consider credit reports when deciding whether to write a policy, and negative credit often can mean higher premiums.\(^3\) Stories on the Internet reveal that romantic partners pull credit reports on each other before agreeing to marriage—and divorce attorneys frequently cajole divorcing spouses to make the revelation of credit reports a condition of dissolution.

The consumer credit industry has long desired the ubiquity of its credit reports. With this desire becoming reality, consumers and industry entities alike are increasingly seeking clarity regarding their rights and duties. Those furnishing credit information as well as those publishing reports containing that information need to know the precise contours of their obligations. Further, consumers need access to judicial remedies if they are unable to correct their reports on their own.

The Ninth Circuit Court of Appeals and the First and Second District of the California Court of Appeal have recently ruled on several unsettled issues that have been the subject of pitched battles in credit reporting cases for the last decade.\(^4\) The Ninth Circuit’s Nelson v. Chase Manhattan Corporation\(^5\) and Gorman v. Wolpoff & Abramson,\(^6\) the First District’s Komarova v. National Credit Acceptance, Inc.,\(^7\) and the Second District’s Sanai v. Saltz\(^8\) are seminal decisions that are a must-know for consumer credit litigators, whether they represent consumers or those involved in any part of the credit industry.

Whether the federal Fair Credit Reporting Act (FCRA) preempts California’s Consumer Credit Reporting Agencies Act (CCRAA) is an issue that was resolved identically in separate decisions by the Ninth Circuit Court of Appeals and by the Second District of the California Court of Appeal. The FCRA substantially preempts state law claims for defamation or invasion of privacy for false credit reporting.\(^9\) It also preempts myriad state laws that specifically provide consumers with the right to pursue actions for false credit reporting against credit bureaus and “furnishers”—defined as debt collectors, or other types of companies and persons, who report derogatory information to credit reporting agencies.\(^10\) However, in the midst of amendments to the FCRA in 1996, Congress exempted from preemption “section 1785.25(a) of the California Civil Code,” the portion of the CCRAA that gives consumers a direct right of action against furnishers of credit information for reporting falsehoods or inaccuracies.\(^11\)

In spite of what would seem to be a clear expression of congressional intent to spare the CCRAA from preemption, particularly as it applies to furnishers, this 1996 amendment spawned more than a decade of contentious litigation over whether or not the CCRAA continued to be preempted. To understand this battle, counsel should be aware of the history of the two acts as well as the differences between them.

The CCRAA\(^12\) was passed in 1975 and has been amended several times since. The act not only addresses identity theft but also credit

Robert F. Brennan is the senior partner of Brennan, Wiener & Associates, in Los Angeles, where his practice focuses on consumer protection matters involving debt collection abuse, wrongful credit damage, identity theft, automobile fraud, and Song-Beverly “lemon law” cases. He coauthored an amicus brief on behalf of the plaintiff/appellant in Gorman v. Wolpoff & Abramson.
report damage and abuse and impermissible access to private credit report information. The CCRAA provides remedies against the major credit bureaus as well as against creditors and debt collectors.

The FCRA \(^\text{14}\) was passed in 1970. Like the CCRAA, it has also been amended several times since, most recently in December 2003. While still entitled the Fair Credit Reporting Act, the newer provisions of the FCRA are known as the Fair and Accurate Credit Trans-

actions Act, or FACTA. The FCRA and the CCRAA share a fundamental legal require-

ment—that creditors and credit reporting agencies pursue “maximum possible accu-

racy” in credit reporting. This remains unchanged under FACTA.

**Private Remedy against Furnishers**

Since their enactment, the FCRA and the CCRAA have provided two remedies for inaccuracies in credit reporting: an individual right to sue credit bureaus (including the major ones—Equifax, Experian, and Trans-

Union) for credit reporting abuse, and a provi-

sion for enforcement by governmental pros-

ecuting bodies. Until the 1990s, no clear private right of action against furnishers was present in either of the acts. This changed in 1993, when the California Legislature amended Civil Code Section 1785.25 to impose sanctions against furnishers of “incomplete or inaccurate” derogatory credit information.\(^\text{15}\) Civil Code Section 1785.31 provides the remedies for any violations of the CCRAA (including those by furnishers), and these include actual damages, attorney’s fees, and punitive damages. With the 1993 amend-

ment, there was no question that the Cal-

ifornia Legislature intended to provide con-

sumers with a private right of action against furnishers.\(^\text{16}\)

Creditors and debt collectors took little time in challenging the new law, claiming that the FCRA preempted the CCRAA. Prior to the amendment, the preemption argument provided a safe harbor for creditors and furn-

ishers, because the FCRA did not provide a private remedy against furnishers. The Second District of the California Court of Appeal addressed the issue in 1995 in *Cisneros v. U.D. Registry, Inc.*\(^\text{17}\) by firmly deciding against preemption. The court relied upon applicable commentary from the Federal Trade Commission (FTC) on the FCRA in reaching its conclusion. *Cisneros* remains good law and not only has never been over-

turned but also has not been distinguished on the preemption issue by any other California court. Nevertheless, it did not lay to rest industry efforts to preempt the CCRAA.

Congress amended 15 U.S.C. Section 1681s-2(b) of the FCRA in 1996 to provide a private remedy against furnishers for report-

ing false or inaccurate credit information. Until this amendment, a consumer damaged by furnisher misconduct could only seek fed-

eral recourse with the FTC. Even after the amend-

ment, furnishers still argued that the FCRA only provided for administrative enforcement by the FTC. The Ninth Circuit Court of Appeals confirmed the FCRA private remedy against furnishers in *Nelson v. Chase Manhattan Corporation*.\(^\text{18}\)

In *Nelson*, the plaintiff appealed the dis-

missal by the district court of his suit under the FCRA for failure to state a cause of action against the creditor, defendant Chase Manhattan Mortgage Corporation. Chase was the furnisher of allegedly false or inaccurate credit information to the three major credit bureaus. The district court held that Section 1681s-2(b) did not create a private right of action for a consumer against a fur-

nisher of credit information, and enforce-

ment was limited to action by the FTC.\(^\text{19}\)

The Ninth Circuit reversed the judgment of the district court and unequivocally held that the primary purpose of the FCRA is to provide a private remedy to injured consumers and to protect consumers against inaccurate and incomplete credit reporting. The *Nelson* court made clear that although Section 1681s-2(a) limits enforcement to governmental bodies, Section 1681s-2(b) was specifically enacted to confer a private right of action to con-

sumers against furnishers of information.\(^\text{20}\) Furthermore, the court held that it is “not for a court to remake the balance struck by Con-

gress, or to introduce limitations on an express right of action where no limitation has been written by the legislature.”\(^\text{21}\)

Section 1681s-2(b)’s private right of action against a furnisher only arises “[a]fter [the furnis-

her receives] notice...of a dispute with regard to the completeness or accuracy of any information provided by a person to a consumer reporting agency.” Under the FCRA, a consumer must first dispute the false or inaccurate credit report information to the credit agency. The credit reporting agency then sends an ACDV (automated dispute verification form) to the furnisher, which is then obligated to investigate the dispute and subsequently instruct the agency to correct the derogatory information, delete it, or keep it without changes. Generally these steps must all take place within 30 days.\(^\text{22}\) If the credit derogatory is not corrected after the 30-day period, then the consumer has a private right of action against both the furnisher and the credit agency.

Thus a consumer’s dispute does not trig-

ger either a duty to reinvestigate or the poten-

tial for FCRA liability unless it is directed at the credit reporting agency. Dispute letters that are sent only to furnishers do not trigger any legal obligation to reinvestigate. Consumers intuitively will dispute a false derogatory from the furnisher but not necessarily with the credit agency. Indeed, consumers have disputed false derogatories sometimes for months or even years with furnishers without trig-

gering any legal duty for the agency to rein-

vestigate.

The CCRAA does not have this type of counterintuitive procedure that the consumer must follow to trigger his or her rights under the statute. If a furnisher provides false or derogatory credit information that damages the consumer, the furnisher may face liabili-

ty. The CCRAA is not, however, a strict lia-

bility statute, since it contains a significant safe harbor in Civil Code Section 1785.25(g): A person who furnishes information to a consumer credit reporting agency is liable for failure to comply with this section, unless the furnisher establishes by a preponderance of the evidence that, at the time of the failure to comply with this section, the furnisher maintained reasonable procedures to comply with those provisions.

Furnishers who “maintain reasonable pro-

cedures” to ensure maximum possible accu-

racy have a valid defense to an action under the CCRAA—in theory. This provision serves the double purpose of providing a safe har-

bor for furnishers while also forcing fur-

nisers to ensure a high level of consumer pro-

tection if they wish to avoid CCRAA liability.

**Preemption Developments**

With the 1996 amendment to the FCRA specifically exempting Civil Code Section 1785.25(a) of the CCRAA, the preemption argument seemingly was dead. However, fed-

eral districts in California faced with resolv-

ing credit reporting disputes after the amend-

ment exempting Section 1785.25(a) began to cite and rely upon *Pulver v. Avco Financial Services*,\(^\text{23}\) a case favoring FCRA preemp-

tion that was decided well before the 1993 CCRAA and the 1996 FCRA amendments. According to *Pulver*, the CCRAA—as it existed in 1986—did not provide for a private right of action against furnishers. To the extent that the 1993 CCRAA amendments expressly created a private right of action against furnishers, *Pulver* should not have been applicable law.

However, in 2000, the U.S. District Court for the Northern District of California relied on *Pulver* in finding FCRA preemption of the CCRAA in *Quigley v. Pennsylvania Higher Education Assistance Agency*, an unpub-

lished decision.\(^\text{24}\) The same district court then proceeded to rely heavily on *Quigley* in 2002 to reach its decision in *Lin v. Universal Card Services Corporation*.\(^\text{25}\) The *Lin* court found preemption of the CCRAA based on its analysis that Section 1785.25 does not create
a private right of action. Lin ignores the state appellate court’s decision in Cisneros, which found against preemption in 1995. The later amendments to the FCRA—which grant a private right of action under Section 1681s-2(b) and carve out a preemption exemption for Civil Code Section 1785.25(a)—do not negate the overall reasoning behind Cisneros that no real conflict exists between state and federal law on this issue. While both the FCRA and the CCRAA have been amended since the Cisneros decision, the key decisional language of Cisneros—that state laws are preempted if inconsistent with the FCRA “and then only to the extent of the inconsistency”—remains valid. Moreover, with the passage of Section 1681s-2(b) providing a private right of action against furnishers under the FCRA, the federal and state statutes have grown more consistent.

Lin also ignores the key language of 15 U.S.C. Section 1681t(b) exempting Section 1785.25(a). This provision exempts the California section “as in effect on the date of enactment of the Consumer Credit Reporting Reform Act of 1996.” Section 1785.25(a) was “in effect” on that date with reference to the remedies found at Section 1785.31; without Section 1785.31, Section 1785.25(a) could never have been regarded as “in effect.” Particularly, it was never “in effect” insofar as creating only a law enforcement remedy, as argued by the Lin court. Trying to pull Section 1785.25(a) away from Section 1785.31, which provides the remedies for violations of Section 1785.25(a), makes no sense whatsoever, particularly since Section 1785.25(a) does not provide for prosecutorial enforcement. Thus the Lin court left Section 1785.25(a) floating in limbo, out of the reach of deserving consumers who were originally intended to receive its benefits.

California’s state appellate courts did not revisit Lin and the preemption issue until this year. However, the Ninth Circuit Court of Appeals spoke first, on January 12, finding against FCRA preemption of the CCRAA. In Gorman v. Wolpoff & Abramson, plaintiff Gorman was an attorney who used his MBNA credit card to pay for delivery and installation of a new satellite TV system. Gorman alleged that the installer, Four Peaks Home Entertainment, botched the installation and damaged his home in the process. Gorman asked for a refund, but Four Peaks refused to provide a refund unless Gorman returned the TV system. Whether Gorman made the TV system available for return to Four Peaks was one of the disputed facts in the trial court.

The matter escalated, and Gorman then notified MBNA that he was disputing the charges. A series of exchanges then ensued between Gorman and MBNA. In August 2003, MBNA removed the Four Peaks charge and related finance charges from Gorman’s credit card bill. However, in October of the same year, MBNA reposed it. In January 2004, following months of Gorman not paying anything on the disputed bill, MBNA reported the debt as a “charge-off” to the credit reporting agencies. Gorman sued MBNA and others for violation of the FCRA and the CCRAA and for libel. The trial court dismissed Gorman’s CCRAA claim as preempted by the FCRA and granted summary judgment on all other claims. Gorman appealed.

After analyzing the FCRA, the Ninth Circuit first embraced the holding in Johnson v. MBNA that a furnisher’s reinvestigation of disputed credit information must be reasonable. The court proceeded to rule that on the specific facts of the Gorman case, MBNA’s reinvestigation was reasonable and thus upheld the trial court’s grant of summary judgment regarding the FCRA claim. The court also held that Gorman had failed to provide sufficient evidence to invoke 15 U.S.C. Section 1681t(e)’s limited exception to FCRA preemption for stating a common law libel claim and upheld summary judgment as to that claim.

On the CCRAA claim, the Ninth Circuit reversed the trial court’s dismissal. The court focused on the fact that Civil Code Section 1785.25 contains no enforcement provision, public or private, so therefore reading Section 1785.25 as entirely disconnected from Section 1785.31 would make no sense. The court focused on the antipreemption language of Section 1681t(a): “No requirement or prohibition may be imposed…with respect to the subject matter regulated under Section 1681s-2 of this title, relating to the responsibilities of persons who furnish information to consumer reporting agencies.” In analyzing the two sections, the court held that only Section 1785.25 imposed a “requirement or prohibition,” whereas Section 1785.31 “provides enforcement mechanisms for ‘requirements or prohibitions’ imposed separately.” Since Section 1785.31 did not impose a “requirement or prohibition,” this section was never preempted by Section 1681t and thus could be used in conjunction with actions for violations of Section 1785.25(a).

The court concluded its analysis by stating that MBNA’s argument that Congress intended to exempt Section 1785.25(a) but not its corresponding remedies in Section 1785.31 made absolutely no sense and would serve no purpose.

Two weeks after Gorman, the Second District of the California Court of Appeal decided Sanai v. Saltz. This case details a long and difficult litigation history between a landlord and a former tenant. Following disputed eviction proceedings, the landlord retained Unlawful Detainer Registry (UDR) to file a credit report of tenant Sanai for unpaid rent. Following UDR’s reporting to the credit bureaus, Sanai suffered adverse credit events, and the protracted and acrimonious litigation ensued.

The court issued a number of rulings on several disputed issues. Its ruling on preemption of the CCRAA was issued before the court reviewed the grant of a judgment on the pleadings regarding Sanai’s CCRAA claim and his common law causes of action. The Sanai court had the benefit of the Gorman decision, which it embraced in its ruling that the FCRA does not preempt the CCRAA with regard to furnisher liability for false credit reporting.

On April 29, 2009, the California Supreme Court denied a petition for review in Sanai. Thus, as 2009 comes to a close, CCRAA claims against a furnisher are viable causes of action within the Ninth Circuit and in California’s Second Appellate District.

Resolving Other Issues

For some time, consumer credit litigators have fought a battle over hearsay and the evidentiary uses of consumer credit reports. Parties have argued that since a credit report is an out-of-court statement, it must be hearsay unless the consumer can provide a witness, such as a qualified person from the credit bureau, to lay a foundation to overcome the hearsay objection. The foundational requirement can become more complicated when third-party vendors sell credit reports to consumers as well as users of the credit reports, such as mortgage companies or investigative services. The consumer credit litigator in some cases has had to lay the evidentiary foundation through a chain of custody going all the way back to the originating credit bureau—a task not necessarily easy or obvious.

In Gorman, the Ninth Circuit addressed this recurring objection and ruled that when a consumer has alleged inaccurate credit reporting, the consumer can testify to the contents of his or her own credit report, since the evidence is not being offered for its truth but for the purpose of showing what is in the credit report. The Gorman court recognized that consumers are often challenging the truth of the contents of a credit report, so the traditional definition of hearsay in the federal and state rules should not exclude a consumer from testifying about a report’s contents. For trial exhibits, however, the consumer credit litigator needs to actually pull credit reports from the credit bureaus that are the sources of the reports, and not from third-party vendors.
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While the Gorman court permits a consumer to testify about the contents of his or her credit reports over a hearsay objection, objections remain regarding lack of foundation and lack of authentication when a consumer credit litigator attempts to introduce third-party vendor reports. If a case depends upon the contents of a third-party vendor report and the third-party vendor is not a party, the consumer credit litigator most likely needs to take depositions of the third-party vendor and the originating credit bureau.

This year the First District of the California Court of Appeal resolved the issue of the applicability of the litigation privilege in identity theft claims. A natural tension exists between laws designed to restrict debt collection abuses and the litigation privilege. In theory, any effort to collect a consumer debt may be headed towards litigation, so the litigation privilege arguably preempts California’s Rosenthal Fair Debt Collection Practices Act.

In Komarova v. National Credit Acceptance, Inc., the plaintiff was harassed repeatedly over a debt that belonged to someone with a similar name. The case recounts the plaintiff’s extensive difficulties in straightening out the problem, which ultimately had to be resolved in litigation against the offending debt collector. The plaintiff prevailed, and the defendant appealed from a verdict finding violations of the Rosenthal Act and for intentional infliction of emotional distress.

The Komarova court then discussed the several specific provisions of the Rosenthal Act that would be rendered meaningless by application of the litigation privilege, and whether it forecloses litigation under the Rosenthal Act. The court relied upon Oei v. N. Star Capital Acquisitions, L.L.C. as the most pertinent precedent:

Applying the [litigation] privilege in this manner would effectively vitiate the Rosenthal Act and render the protections it affords meaningless. As there appears to be no way to reconcile the statutes [litigation privilege and the Rosenthal Act], the court applies the familiar principle of statutory construction that, in cases of irreconcilable conflict, the specific statute prevails over the general one.

The Komarova court then discussed the several specific provisions of the Rosenthal Act that would be rendered meaningless by application of the litigation privilege, and ruled that the Rosenthal Act is the more specific statute. Thus, the litigation privilege does not invalidate claims under the Rosenthal Act. However, the court held that the litigation privilege would bar claims arising out of wrongful debt collection for intentional infliction of emotional distress.

Consumers and the credit industry will
reap benefits from these important decisions, which bring clarity to this important area of the law. Still, however, the economic downturn has brought more credit reporting issues to the fore—including those involving class actions and individual actions—and these, too, will require the attention of courts for their resolution.

2 Congress emphasizes the importance of the Fair Credit Reporting Act in its preamble: “The banking system is dependent upon fair and accurate credit reporting. Inaccurate credit reports directly impair the efficiency of the banking system, and unfair credit reporting methods undermine the public confidence which is essential to the continued functioning of the banking system.” 15 U.S.C. §1681a(1).
4 Attorneys representing consumers and businesses are increasingly discovering that “credit damage” covers claims involving personal injuries, wrongful foreclosures, wrongful debt collections, landlord-tenant disputes, and ordinary business conflicts.
5 See Robert F. Brennan, Faith and Credit, LOS ANGELES LAWYER, Nov. 2004, at 36 (discussing erroneous court decisions holding that the federal FCRA preempted California’s CCRAA).
6 Nelson v. Chase Manhattan Corp., 282 F. 3d 1057 (9th Cir. 2002).
13 Civ. Code §§1785 et seq.
16 It is important to note that Civil Code §1785.25(a) has always provided for a private right of action and was not passed with the intention of being applicable only under the auspices of public prosecutorial bodies.
18 Nelson v. Chase Manhattan Corp., 282 F. 3d 1057 (9th Cir. 2002).
19 The parties in Nelson did not dispute that the FCRA creates a private right of action against credit bureaus, such as Experian and TransUnion. Nelson dealt exclusively with whether the FCRA created a private right of action against a furnisher.
20 Nelson, 282 F. 3d at 1060.
21 Id. The limitation refers to 15 U.S.C. §1681s-2(d), which restricts enforcement of 15 U.S.C. §1681s-2(a) and (c) to public prosecutors. The Nelson court correctly read §1681s-2(d) as not restricting 15 U.S.C. §1681s-2(b) to governmental enforcement.
26 Id. at 1152-53 (citing Quigley, 2000 U.S. Dist. LEXIS at *8).
29 In credit industry parlance, a “charge-off” refers to the lender declaring the debt as a loss in its financial records. A charge-off does not relieve a consumer of the obligation to pay the debt.
30 Johnson v. MBNA, 357 F. 3d 426 (4th Cir. 2004).
31 15 U.S.C. §1681t(b)(1)(F) (emphasis added); Gorman, 552 F. 3d at 1030.
32 Gorman, 552 F. 3d at 1031.
33 Id.
35 The Unlawful Detainer Registry is a smaller credit bureau used primarily by residential landlords to record and track evictions and problem tenants.
36 Gorman, 552 F. 3d at 1024.
37 FED. R. EVID. 807(a); EVID. CODE §1200(a).
38 Civ. Code §§1788 et seq. See Action Apartment Ass’n, Inc. v. City of Santa Monica, 41 Cal. 4th 1232, 1251 (2007) (“A prelitigation communication is privileged…when it relates to litigation that is contemplated in good faith and under serious consideration.”).
40 Civ. Code §547.
42 Id. at 1100.
43 Komarova, 175 Cal. App. 4th at 340.
44 Id. at 341-43

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When Transactional Attorneys Face Criminal Liability

WHEN IT COMES TO PROSECUTING big-firm transactional attorneys, the notion that a "law degree, like some sorcerer’s amulet, can ward off the rigors of the criminal law," simply is not true. Lawyers are expected to have a comprehensive understanding of the law and thus are held to an even higher standard than other professionals regarding criminal conduct. Nothing about graduating from a top law school or practicing at a prominent national law firm insulates attorneys from criminal liability in connection with their clients’ wrongdoing. This is confirmed by the recent spate of federal criminal filings against transactional attorneys who, the government contends or has proven, aided and abetted the criminal endeavors of clients.

For example, in 2007, Joseph P. Collins, head of the derivatives practice group at his law firm, was charged with helping to hide the debts of his client Refco, a futures and commodities broker that went public and collapsed in 2005. Collins was accused of helping Refco hide more than $1 billion in debt by drafting loan agreements to conduct “round trip loan transactions” that temporarily transferred Refco’s losses from its books at the year’s end, giving the impression that Refco was a profitable company.2

According to the indictment, in the late 1990s Refco transferred huge trading losses to its parent RGHI and then carried out transactions to conceal the extent of its parent company receivables from auditors. For example, in February 2000, approaching the end of Refco’s fiscal year, three customers lent $310 million to RGHI, which RGHI then used to pay down its obligations to Refco. At the same time, Refco lent the three customers $310 million. As a result, it appeared on Refco’s books that Refco had approximately $310 million in receivables from the three legitimate, arm’s-length customers, and the debt from RGHI appeared to be reduced by $310 million. In March 2000, the transactions were reversed, with Refco lending the same $310 million back to RGHI, which it used to pay back the three customers.

The indictment charged that Collins and attorneys working at his direction were responsible for drafting the legal documents that effected the transactions, and that Collins’s status as a partner in a well-known law firm furthered Refco’s scheme by helping third parties to feel comfortable participating in them.3 Collins allegedly billed more time to Refco than to any other matter, generating $40 million in fees for his firm through the engagement.4 Prior to trial, Collins remained free on $1 million bail, while his law firm placed him on leave.

During days of testimony at trial, Collins asserted on the stand that he was an innocent victim of the Refco fraud, that Refco officials had lied to him, and that he was unaware that Refco had been parking its debt at RGHI. Collins further testified that he had delegated to an associate at his firm the work involving the back-to-back loan transactions, which he described as routine. In June, Collins was found guilty of a number of counts of fraud, money laundering, and making false filings to the Securities and Exchange Commission. Collins resigned from his law firm. He faces a maximum sentence of 85 years. In reference to the indictment, the prosecutor explained, “It is not a crime to have a client who commits a crime; no lawyer will be prosecuted unless the lawyer knows about his client’s fraud and agrees to join in it understanding its unlawful nature."5 At trial, the prosecutor told the jury that Collins had a motive to lie for Refco: It was his biggest client from 1997 until its collapse.6

Tax Fraud

In October 2005, Raymond Ruble, a tax partner at a prominent law firm, was charged along with partners of the accounting firm KPMG with conspiring to defraud the IRS by devising, marketing, and implementing a series of fraudulent tax shelters.7 Ruble was alleged to have provided clients with letters that falsely stated that the tax benefit “was more likely than not” to survive IRS challenge, thereby allowing the clients to avoid IRS penalties in the event the IRS disallowed the tax benefits. However, according to the indictment, Ruble knew the tax positions taken were not more likely than not to prevail against an IRS challenge, as there was no reasonable likelihood for profit, and that the opinion letters were fraudulent in that they misleadingly described the scheme as an investment program when it was in fact merely a vehicle to generate phony tax losses.8

The indictment further alleged that Ruble’s law firm earned gross fees totaling more than $23 million. While the case against a number of Ruble’s alleged coconspirators was dismissed due to government misconduct, Ruble was found guilty of multiple counts of tax evasion and was sentenced to 78 months in custody. In sentencing Ruble and his codefendants, Judge Kaplan stated, “[T]hese defendants were not prosecuted and they were not convicted for making mistakes in judgment on debatable questions in good faith,” adding, “these defendants knew that they were on the wrong side of the line.”9 Ruble has been dismissed from his law firm and suspended from the practice of law. His case is currently on appeal.

In June, the government filed a similar indictment against, among others, tax attorney Paul Daugerdas, a partner at a now-defunct firm (that entered into a nonprosecution agreement with the government), and attorneys at BDO Seidman.10 The indictment alleges that these attorneys entered into an alliance to design, market, and implement tax shelters, refer clients to purchase these tax shelters, and prepare returns reporting the tax benefits arising from those tax shelters.

According to the indictment, from 1998 through 2002, the seven named defendants collectively earned $180 million from the sale of these tax shelters to their clients, and Daugerdas’s firm made $230 million in fees from selling the shelters to clients.11 A spokeswoman for Daugerdas told the Wall Street Journal that he “firmly believes that the tax advice provided to his clients was well within the scope

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of then-existing federal tax law.”12 Three people already have pleaded guilty in connection with the case.

In fall 2007, Martin Weissberg, a securities lawyer and partner of a prominent national law firm, was charged with conspiring with two of his corporate clients’ principals to facilitate short-swing sales in his clients’ stock and commit a fraud on the shareholders of his two corporate clients.13 Through private investment in public equity (or PIPE) transactions, two investors acquired large amounts of stock in companies Weissberg represented, and, in the names of a series of nominees, entered into short sales of the companies’ stock, anticipating the stock price would fall. Once the companies’ registration statements reporting the PIPE transactions became effective, the market price fell as anticipated, and the investors cashed in on their short sales, reaping more than $55 million in profits.

According to the government, Weissberg facilitated what these investors were doing by lying to the SEC and the company’s auditors. In particular, the government charged that in a series of filings that Weissberg either authored or reviewed, several aspects of these transactions were not, but should have been, disclosed to the SEC, including the fact that the nominees were controlled by the investors, the fact that the investors held more than 5 percent beneficial interests in each of the companies’ stock, and the fact that the nominees were related to one another, because they were all controlled by the same two investors. For his efforts, Weissberg allegedly received $1.7 million in kickbacks. He awaits trial on charges of conspiracy to commit securities fraud and money laundering. After his indictment, and despite his not guilty plea, Weissberg’s law firm requested and received his resignation.

While these lawyers may be vindicated at trial or on appeal, the circumstances resulting from their indictments and trials—which at the least include being placed on leave or dismissed by their firms and having their reputations destroyed—warrant an examination of what lesson attorneys can learn from their downfalls.

Intent
The lesson begins with basic criminal law. If the government can establish 1) the client’s fraud and 2) that a lawyer acted in furtherance of the client’s fraud, the question of the lawyer’s guilt depends on whether the attorney knew of the client’s fraud while acting in furtherance of it. The question thus becomes: Did the lawyer act with the requisite criminal intent by knowingly joining in and furthering the client’s criminal conspiracy, or was the attorney merely the client’s unwitting dupe?

Collins serves as an example: The government asserts that the client’s agreements, prepared at Collins’s direction, were a fraud on the company’s auditor. Clearly, Collins acted in furtherance of this fraud by drafting the client’s agreements. The only question is whether Collins was aware of the fraud and therefore acted with intent to further it. At trial, the government argued that he did. His lawyer, on the other hand, asserted that he did not know or understand the fraudulent nature of Refco’s goals but rather was simply documenting his client’s transactions.

The line between faithful execution of a client’s desires and criminal fraud is crossed when the lawyer has knowledge of the client’s criminal objective. On one side of the line are attorneys who understand what their clients are up to and make a conscious choice to further the illegal plans of their clients. On the other side are lawyers who document one part of a transaction without knowing the client’s fraudulent objective. This explains why many attorneys at the firms that worked on the cases discussed above were not indicted.

If Collins had been asked only to document, in isolation, a transaction in which Refco lent $310 million to three clients, he would have had nothing to suspect. But if it is clear to an attorney that a transaction has no economic substance, the lawyer must carefully consider the purpose of the transaction that he or she is being asked to document, as well as the client’s purpose in pursuing it.

Knowledge
For an attorney in Collins’s position, the question is: How much do I need to know? Lawyers who only recall their law school ethics class and not their criminal law class may be surprised to learn that the degree of knowledge required to violate the criminal law may be the same as or lower than that required to violate ethics rules. The American Bar Association’s ethics rules (adopted in all jurisdictions except California, Maine, and New York) prohibit lawyers from counseling clients “to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent....”14 California’s ethics rules do not specifically address this issue but note that when seeking guidance on professional conduct, “[e]thics opinions and rules and standards promulgated by other jurisdictions and bar associations may also be considered.”15 The ABA’s ethics rules define “knowledge” to “denote actual knowledge of the fact in question.”16 Attorneys who know that the conduct a client proposes is illegal are prevented by ethics rules from assisting the client in the venture.

The criminal standard may be lower. Under federal securities law, the government must prove that the defendant acted “willfully.”17 The government does not need to prove knowledge of illegality;18 rather, its burden is satisfied by proving a defendant’s “general awareness of wrongful conduct which may exist even if a defendant believes his chicanery is in technical compliance with the law.”19 A defendant also can willfully violate securities law by acting with reckless indifference to the truth of statements made in the course of the fraud.20 While actual knowledge of the illegal nature of the client’s conduct is required for an ethics violation, it is not required in order to prove that a crime has been committed.

Can a lawyer, knowing where the line is, take steps to maintain plausible deniability? Can a lawyer who is approached to document a short-term $310 million loan not ask the client why the company wants to do this deal and thereby avoid learning that this loan is only a part of a complicated transaction designed to conceal huge losses from auditors or investors? First, if the attorney consciously avoided learning the information, that itself may fulfill the criminal intent requirement necessary for many criminal violations.21 In fact, in denying Ruble’s motion for judgment of acquittal, Judge Kaplan concluded that the jury had been presented with sufficient evidence to find that Ruble acted willfully either by virtue of his knowledge of the transaction at issue or by consciously avoiding facts relating to that transaction.22

The attorney’s only legal defense would be that he negligently or reasonably avoided learning the information. But is that assertion likely to be believed? Will prosecutors and jurors believe that an attorney who has a confidential relationship with a client did not know the full scope of the client’s objectives? The ABA’s ethics rules virtually presume that the attorney has this knowledge, requiring attorneys to provide competent representation, which is defined as “inquiry into and analysis of the factual and legal elements of the problem, and use of methods and procedures meeting the standards of competent practitioners.”23

Because attorneys are expected to have knowledge of their clients’ affairs and the relevant facts behind their clients’ purposes, it may be difficult for an attorney to convince prosecutors or jurors that he or she was unaware of a client’s illegal objective. This is even more likely to be the case if a substantial portion of the attorney’s billings is devoted to that client.

Of the attorneys who can get charged, which actually do get charged? The indictment against Collins alleges that the transactions at issue were memorialized in loan agreements prepared by “attorneys working at Collins’ direction.”24 The Weissberg indictment charges that “Attorney — 1”...
prepared public filings that omitted material information and that Weisberg reviewed them. Assuming these unnamed attorneys were familiar with the omitted information, they would appear to be as prosecutable as Collins and Weisberg, but they were not charged.

**Discretion**

While it is certainly possible that one or more attorneys who worked for the defendants turned state’s evidence, there nonetheless appear to be myriad other attorneys that, in the exercise of the broad discretion granted prosecutors, were not charged. How do prosecutors exercise their discretion? The indictments in these cases contain some seemingly superfluous allegations that may explain who gets charged and who does not. By referring to the amount of fees Collins and Ruble generated for their respective firms as opposed to the monies each personally earned as a result of the representation, the prosecutors seem to be suggesting that these representations were critical to the lawyers’ stature within their firms and that they committed these acts in an attempt to hold on to that status. Collins’s prosecutor argued at trial that Collins engaged in the alleged conduct because Refco was the most important client relationship he had at the firm.

In these cases, the prosecutors appear to have exercised their discretion to charge only the relationship partner and spare the firm’s other partners, who worked on the files and shared in the ill-gotten fees, and the firm’s associates, who certainly worked on the files and whose salaries were paid out of the ill-gotten fees. While this may prove nothing more than that power comes with a bull’s-eye, it is sobering to realize that many of the attorneys who worked on these files could have been charged.

Finally, one should consider what a transactional attorney is to do when approached by a client, a colleague, or a superior to do something that would be against big-firm transactional attorneys’ interests or her observations. Ethics rules make with one’s eyes at the discretion of prosecutors who may be looking to establish theirs.

First, there may be little room for an attorney to convincingly argue that he or she did not understand the nature of the client’s goals and therefore did not know the client’s goal was fraudulent. Considering the billing rates of big-firm attorneys (including relatively junior ones), and the expertise and competency that justifies those rates, even if the lawyer did not in fact understand the client’s goals, that assertion may not be convincing.

The only way to defeat an argument that the attorney consciously avoided learning the information, or manifested a reckless disregard for the veracity of the representations being made on the client’s behalf, is for an attorney actually to ask for the information and to obtain it. In other words, an attorney’s only safe course is to ask the hard questions and get complete answers. In the criminal arena, what attorneys do not know can hurt them.

Second, when an attorney has concerns regarding the legality of the client’s transactional goals, what are the attorney’s options? An attorney whose expertise may be limited to a particular area of the law should consider reaching out to another lawyer in his or her firm, or a criminal defense attorney for legal advice on a particular situation. Ethics rules permit this either explicitly or implicitly.

Junior lawyers acting at the direction of senior ones may need to discreetly seek third-party advice. While a junior lawyer is offered some protection from attorney discipline under, for example, Rule 5.2(b) of the ABA Model Rules of Professional Conduct, which permits a junior lawyer to act in accordance with a supervisory lawyer’s reasonable resolution of an arguable question of professional duty, there is no “just following orders” defense to a criminal charge.

If a lawyer cannot comfortably accept that a transaction is permissible, he or she needs to get off the case. For a junior lawyer this may be as simple as getting assigned to a different matter; for a key partner, this may require firing the client. While there is no doubt that either of these scenarios may prove costly to the lawyer in terms of reputation and prestige, the alternative—getting criminally charged for a client’s misdeeds—is far worse.

In each of the cases discussed, the attorney has been charged with conspiracy for joining in and acting in furtherance of the client’s illegal scheme. Had the attorneys charged in those cases withdrawn from the representation, they could have asserted that act of withdrawal as an affirmative defense to the conspiracy charge, and most likely they never would have been charged. Even though Ruble was ultimately acquitted of the conspiracy charge, that is small solace for a lawyer facing 78 months of imprisonment. If an attorney does withdraw, it is worth bearing in mind that some jurisdictions may require the withdrawing attorney to report his or her observations. Ethics rules make withdrawal permissive; criminal law makes it mandatory.

While some perhaps still cling to the notion that the criminal law is reserved for back-alley drug deals, recent criminal filings against big-firm transactional attorneys make clear that transactional attorneys need to be aware of the criminal law implications of their clients’ requests. They should also consider a jury’s likely reaction to the defense
argument, “I didn’t know my client was engaged in criminal wrongdoing when I wrote the contracts and my law firm made millions.” Attorneys cannot bury their heads in the sand. They have no choice but to learn the facts, and if all is not right, get off the case. If a transaction’s legality remains unclear, the option of consulting a criminal law expert during the engagement is far preferable to the requirement of hiring one after the fact.  

1 United States v. Cantolo, 818 F. 2d 980, 996 (1st Cir. 1987).
2 United States v. Collins, 07-01170 (S.D. N.Y.), Indictment ¶34.
3 Id. at ¶10.
4 Id.
6 Mark Hamblett, Mayer Brown Partner Convicted in $2.4 Billion Refco Fraud, N.Y. L. J. (July 13, 2009).
7 United States v. Stein, 05-CR-0888 (S.D. N.Y.), Superseding Indictment.
8 Id. at ¶40(a), (d).
11 Id. at ¶¶59, 60.
12 Chad Bray, In BDO Case, 7 Charged with Fraud, Wall St. J., June 10, 2009.
14 MODEL RULES OF PROF’L CONDUCT R. 1.2(d).
16 MODEL RULES OF PROF’L CONDUCT R. 1.0(f).
18 United States v. English, 92 F. 3d 909 (9th Cir. 1996).
19 United States v. Chiarella, 588 F. 2d 1358, 1371 (2d Cir. 1978).
20 Tarallo, 380 F. 3d at 1189 n.5; cf. RESTATEMENT OF THE LAW THIRD, THE LAW GOVERNING LAWYERS §54 cmt. g (2000) (“Mere suspicion on the part of the lawyer that the client might intend to commit a crime or fraud is not knowledge.”).
21 United States v. Benjamin, 328 F. 2d 854, 862 (2d Cir. 1964).
23 MODEL RULES OF PROF’L CONDUCT R. 1.1 cmt. 5.
26 While the State Bar of California provides practitioners with an ethics hotline, it cannot provide legal advice.
27 MODEL RULES OF PROF’L CONDUCT R. 1.6(b)(4) cmt. 9.
28 EVID. CODE §912(c) (A disclosure that is itself privileged is not a waiver of any privilege.), §912(d) (A disclosure in confidence of a communication that is protected by a privilege is not a waiver of the privilege when disclosure is reasonably necessary for the accomplishment of the purpose for which the lawyer was consulted); see also San Diego Cty. Bar Ass’n Ethics Op. 1996-1.
29 MODEL RULES OF PROF’L CONDUCT R. 1.16; CAL. RULES OF PROF’L CONDUCT R. 3-700(C)(1)(b),(c).
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Giving and RECEIVING

Courts will appoint receivers only if strict statutory requirements are met

AT THE HEIGHT OF THE REAL ESTATE BOOM, borrowers found it easy to fully leverage their real property. Now, with real property prices dropping fast, mortgages remaining the same, and full payment of interest-only mortgages due or accelerated, many borrowers find themselves underwater along with their once seemingly stellar investment. The parties who are typically affected by this turn of events are senior secured lenders, borrowers, junior secured lenders, unsecured creditors, and guarantors. As real property disputes among these parties evolve into litigation, courts may appoint a receiver to manage and preserve the property pending the outcome of the dispute.

With the growing need for real estate receivers, real estate attorneys should understand how a receiver is appointed, what a receiver’s powers and functions are, and the range of practical and legal issues that may arise in a real estate receivership. Those typically asserting the statutory grounds to seek the appointment of a receivership are secured lenders. Practitioners representing secured lenders need to be alert to a variety of issues and should carefully tailor the appointment order to best preserve their clients’ interests.

A court appoints a receiver as an officer, representative, or agent of the court\(^1\) to 1) take possession of property that is the subject of litigation, 2) manage the property, and 3) preserve it and sell it—all subject to and in accordance with court orders.\(^2\) A court’s jurisdiction to appoint a receiver is an ancillary equitable remedy to an underlying suit\(^3\) and is governed by statute. Receivers cannot be appointed by an arbitrator or by stipulation of the parties involved.\(^4\)

When a borrower is in default of its loan, two statutory grounds to seek a receivership appointment come into play. The first is for the preservation of real property during a judicial or nonjudicial foreclosure “where it appears that the property is in danger of being lost, removed, or materially injured, or that the condition of the deed of trust or mortgage has not been performed, and that the property is probably insufficient to discharge the deed of trust or mortgage debt.”\(^5\) The second is “[t]o protect, operate, or maintain real property encumbered by a deed of trust or mortgage to collect rents” in connection with a secured lender’s action for specific performance on

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an assignment-of-rents clause. A receiver will not be appointed by the court unless the parties prove that the statutory requirements are strictly met. Parties can seek to prove that the property is in danger of being lost, removed, or materially injured by showing significant mismanagement or failure to maintain the property, collect rent, and pay real estate taxes.

A receiver’s powers and functions are not only granted and controlled by statute but also by the order of appointment and by orders subsequently made by the court. Although a receiver may take actions without prior court approval and seek court approval later to limit the receiver’s liability in case the court disapproves of the receiver’s course of action, a receiver should obtain specific instructions and orders from the court regarding any authority not expressly conferred by statute or the order of appointment. If a court disapproves of the receiver’s action, any contract entered into by the receiver becomes the personal obligation of the receiver and is not binding on the receivership estate.

The general statutory powers of a receiver, which are all subject to the control of the court, are:

1. The power to bring and defend actions.
2. The power to take and keep possession of property, receive rents, collect debts, and make compromises regarding the same.
3. The power to make transfers.
4. The power “generally to do such acts respecting the property as the court may authorize.”
5. The power to sell property with court approval upon prior notice to interested parties and subject to court confirmation.

The fourth general power is the key statutory provision that makes the order appointing the receiver critical, because the order can either expand or limit a receiver’s statutory powers.

**Drafting the Order of Appointment**

After the court initially appoints the receiver, the receiver or other parties may apply to the court during the case to obtain further orders and instructions regarding the receiver’s powers in administering the estate. Practitioners who understand precisely what an order appointing the receiver should contain will realize savings in time and money because future trips to the court requesting more appointment powers will not be necessary.

Prior to drafting the order, counsel should be aware of all the facts of the case, precisely what the receiver will possess, and what property will be administered. For practitioners representing secured lenders, reviewing the loan documents is critical to ensure they include all the lender’s collateral, including the borrower’s pledged personal property, not just the real estate subject to the receivership. The party seeking the receiver may nominate the proposed receiver candidate. The moving party’s nominee is generally appointed by the court, assuming the nominee is qualified. It may be helpful to contact the proposed receiver in advance to discuss the contents of the order.

Appointment orders should contain several critical provisions:

- Possession of the property should vest immediately in the receiver, including bank accounts, payment rights, cash on hand, and all subsequently obtained property, such as rents improperly paid to defendants postreceivership.
- The borrower and other third parties should have an affirmative duty to 1) deliver keys, access codes to the property, bank accounts, payment rights, security deposits, and cash on hand to the receiver, and 2) cooperate with the receiver in the administration of the receiver’s powers and duties.
- The borrower must disclose and deliver to the receiver all records relating to the receivership assets, such as rent or tenant rolls; leases; inventories of furniture, fixtures and equipment; related maintenance or other records; vendor and maintenance contracts; and insurance and utility information. If the property is a construction project, the duty to disclose and deliver should include 1) all plans, specifications, and cost sheets, 2) all bids and contracts for construction of improvements, 3) all invoices, billing statements, preliminary notices, liens, and related documents for contractors and subcontractors, and 4) all licenses, building permits, and other governmental approvals associated with the project.

The order also should enumerate the actions that the receiver is authorized to undertake. The receiver must be able to:

- Assume or reject existing contracts and leases.
- Enter into new contracts and leases, including contracts to insure, maintain, and protect the collateral.
- Preserve and maintain the property, including making necessary repairs or completing construction.
- Pay ordinary expenses incurred in connection with preserving and maintaining the property, such as taxes, fees, mortgage debt, and receiver’s fees and costs.
- Engage employees and agents, such as property managers and accountants, and set their compensation in the ordinary course of maintaining, preserving, and collecting collateral from estate assets.
- Compromise claims.
- Sell the property with further court approval.
- Employ legal process and engage counsel to represent the receiver in protecting the property and intervening in existing actions in which the borrower is involved.
- Enjoin the borrower and its agents from disturbing the receiver’s possession of the property and taking actions that may diminish the value of the property.
- Perform an environmental assessment of the real property, because lenders do not want to take possession of environmentally contaminated property.

The appointment order should further specify that the appointment of a receiver does not prejudice the lender’s right to assert other remedies allowed to the lender under loan documents or applicable law.

**Preserving and Managing the Property**

A receiver has the duty to manage and preserve the property. The functions of the receiver in carrying out this duty may vary based on the type of property subject to the receivership. If the property is income-producing, the receiver’s key function will be the collection of rents and ensuring that conditions at the property maximize the property’s revenues. If the property needs maintenance or repairs, tenants are offsetting rent payments because of the poor physical condition of the property, or new tenants are hard to attract because of the property’s condition, then the receiver can make improvements to the condition and management of the property—subject to the availability of revenues or the secured lender’s willingness to fund them. In residential properties, receivers can resolve health and safety code violations that might otherwise create risks or liability for the secured lender after foreclosure.

Unless the repairs required are substantial and could be considered “capital improvements,” the receiver’s general authority under applicable statutes and the appointment order should allow the receiver to make the necessary repairs. For example, a court order may provide that repairs and improvements in a stated aggregate amount may be made without notice or further court order. If the receiver makes “unreasonable improvements” to the property, the receivership estate would be liable for the expenditure. If the property does not produce enough income for the receiver to make repairs or capital improvements, the lender or receiver may need to obtain additional court orders to approve advances of funds or borrowings supported by receiver certificates. The court order can allow the use of receivership certificates, which evidence the debt and become a first lien on the property.
If a property is under construction when the receiver takes possession, or the property is a commercial income-producing project for which the tenant improvements to be made are covered under existing leases, then the party seeking the receiver has a couple of options for addressing these issues. The party should consider whether the appointment order should grant the receiver expansive authority to make repairs or require the receiver to obtain additional instructions and orders of the court to address construction and management issues after the receiver has taken possession.

To determine whether a receiver should be authorized to complete the construction required for a project or a tenant improvement, the lender may seek to obtain an independent valuation or appraisal of the property in its “as is” condition. However, the value of the completed property may not be available at the time of the receiver’s appointment. The as-is appraisal will require a detailed, comprehensive breakdown of costs and the timing of completion and sales. Until the receiver takes possession of the property and completes a thorough inspection, the lender will likely have insufficient information to fully ascertain the needs of the project, prioritize any repairs or construction goals, assess the duration of the receivership, and determine what should be accomplished on the project during the receivership. If the receiver is charged with completing the construction, the appointment order should address the issues of construction funding, costs and timing of completion, timing of likely sales and cash flow, existing and potential future mechanic’s liens, lender’s advances, receiver’s certificates for borrowing, and risks of defective work or other disputes.

In addition, the receiver must pay expenses and taxes. The receiver is responsible for collecting income from the property and paying expenses incurred after commencement of the receivership, not before, unless the court authorizes payment of prereceivership claims or prereceivership expenses must be paid to preserve the property. For postreceivership activities, the receiver may make motions to the court for instructions and to obtain additional, express review and authorization.

Of course, the receiver should not be running into court repeatedly to obtain “comfort” orders when management activities have already been approved, because this increases attorney’s fees and costs paid from receivership assets—that is, the lender’s cash collateral. On the other hand, the receiver is justified in seeking further instruction or approval if its activities would have a material impact on the assets or the case.

For example, a receiver managing a 100-unit apartment complex would most likely have the general authority to enter into a handful of new short-term leases (typically six months to one year). However, for a receiver managing a shopping center, entering into a long-term lease with a new anchor tenant is an act that would have a material impact on the property. The lease must be presented for specific approval through a motion for instructions. A receiver managing a construction project can proceed with minor work in progress without approval, but major tenant improvements under a lease would require further approval.

Generally, for prereceivership debts, secured lenders do not want their cash collateral used for paying unsecured creditor claims, unless the receiver wants or needs to continue doing business with the creditor parties (such as utility companies, subcontractors to a construction project, vendors that supply goods and services to the property, or vendors that maintain and operate the property) after the receivership. Also, depending on the facts of the case and the appointment order, receivers may deviate from the norm and pay other secured lenders. Paying those debts arguably “preserves” the property because it avoids accrual of higher default interest and late charges and increases the equity available in the property. Real property taxes usually are paid because they are a senior lien, and early payment avoids further accruals of interest and penalties.

Secured lenders should remember that until a foreclosure sale is completed or a judgment is entered, borrowers own the property. Moreover, borrowers as well as guarantors have a significant interest in the management of the property as well as decisions made regarding it because these actions have an impact on their liability. Given the current downturn in the real estate economy and the increasing number of troubled banks, it would not be surprising to see more borrowers asserting lender liability claims. Further, not every lender will be able to complete a judicial foreclosure or court-approved sale,
The program services listed to the left are provided by the four LACBA public service projects (Barristers AIDS Legal Services Project, Dispute Resolution Services, Inc., Domestic Violence Project, and Immigration Legal Assistance Project) and more than 20 other law-related charities located throughout Los Angeles County.

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A Special Tribute to Linda Stude

The Los Angeles County Bar Foundation wishes to acknowledge and pay special tribute to Linda Stude, who will be retiring within the next few months, for her 22+ years of dedication and devotion to the Foundation.

During her tenure, Linda has worked with many volunteer Board members, staff, and scores of law-related non-profits seeking funding from the Foundation. Due in large part to Linda’s diligence and ability to motivate donors and volunteers alike, the Foundation has distributed grants totaling more than $6.2 million since the 1988 grant year.

If you plan to donate and would like it to be a tribute to Linda Stude, please indicate on your check “Linda Stude Tribute.” On-line credit card donations may also be made in Linda’s honor at www.lacbf.org (click on DONATE NOW).
or obtain judgment in the typical four-month period for nonjudicial foreclosure sales, so the receiver may operate the property for quite a while.

**Selling the Property**

A receivership is considered a prejudgment remedy to protect and preserve the property subject to dispute during the pendency of a case until judgment or a nonjudicial foreclosure. The receiver therefore cannot sell the property under receivership without express authority of the court—and this authority is not always granted. Absent a showing that selling the property is necessary, the receiver cannot sell the property against the will of any of the disputing parties until the conclusion of a trial on the merits of the underlying dispute.

For example, in *Cal-American Income Property Fund VII v. Brown Development Corporation,* a receiver was appointed during a dispute between a buyer and seller of commercial property. The buyer wanted to retain the property and recover damages, and the seller wanted to rescind the sale. With the seller’s support and over the buyer’s objections, the receiver sought to sell the property. The court held that the property could not be sold because the receiver did not present any evidence demonstrating “actual...necessity for the sale.” According to the evidence, the property generated enough income to pay operating expenses, and the property was not in danger of being lost to creditors. The goal of the buyer was not to obtain the cash value of the property but instead to continue to retain ownership of the property. Thus, the court held that the sale was “manifestly” unfair because the receiver failed to demonstrate the need for an immediate sale of the property.

Courts may authorize a sale if the parties can show some benefit to constituents of the receivership estate other than the secured lender. However, the support of the secured lender for the sale is an important consideration. In *Resolution Trust Corporation v. Bayside Developers,* the defendant Bayside obtained a construction loan for the construction and sale of multifamily condominiums and single-family residences. The loan documents contained a release clause that applied to the sale of each completed unit. When Bayside defaulted on its loan, some completed units were in escrow. The court appointed a receiver, who closed the escrows, sold the model unit furniture, and turned over a portion of the proceeds to the lender in accordance with the court’s instructions. On appeal, the court held that “the goal of Bayside’s condominium project was development and sale of townhomes.”

The receiver’s actions—selling the townhomes and turning over the proceeds to the lender—were consistent with the receiver’s powers under the appointment order.

**Bankruptcy and Other Issues**

When a borrower files for bankruptcy, the secured lender may not seek appointment of a receiver until after the lender obtains relief from the automatic stay from the bankruptcy court. If a receiver was appointed before the borrower files for bankruptcy, then the receiver must turn over possession of property and any rents or proceeds arising from the property to the bankruptcy trustee or the debtor in possession and file an accounting of the rents and proceeds that came into the receiver’s possession during the receivership.

The receiver can be excused from turning over the property and rents and may remain in possession postbankruptcy if the secured lender can demonstrate that the interests of creditors “would be better served” by the retention of the receiver. The bankruptcy court makes a determination whether creditors’ interests are better served by a receiver remaining in possession by reviewing a number of factors, including the condition of the property, whether the borrower has committed fraud or mismanaged the property, and the length of time the receiver has been in possession administering the property. However, if the receiver has not yet taken possession of the property at the time the bankruptcy petition is filed, the receiver can no longer do so because, under the Bankruptcy Code, no grounds exists for the receiver’s appointment—even if the appointment order was issued prior to the bankruptcy filing.

A party seeking a receiver’s appointment and the receiver cannot directly or indirectly make prereceivership contracts or understandings because the receiver is supposed to be an agent of the court. A receiver and a party cannot agree on how the receiver will administer receivership assets, how the receiver will charge or pay for services concerning receivership assets, or what capital expenditures will be made on the property. Similarly, a receiver cannot make agreements concerning postreceivership management of assets.

Tension may exist between the role of the receiver as a neutral and the interests and goals of the secured lender. While the receiver must act independently and cannot take direction from a secured lender, lenders have an indirect influence on the receiver. This is because lenders typically set in motion the appointment of the receiver, and lenders are usually financial institutions with many real estate loans that may default and require the appointment of a receiver. As a practical matter, this tension generally is more theoretical than real because the goals of the secured lender—such as making necessary repairs, increasing equity in the property, minimizing payment of penalties and interest, instituting proper management to maximize rents, and protecting the property from further loss or deterioration—are all consistent with the proper role and function of a receiver as well as the interests of the borrower parties.

A receiver holds property subject to the rights of any parties who have a superior interest in the property, even if those parties are not part of the litigation giving rise to the appointment of the receiver. But if a party with a superior interest wants to intervene in the litigation or to institute a separate legal action, the party must seek prior court approval.

When a borrower defaults on a mortgage, a receiver is only authorized to take possession of property that is subject to the lien. If the receiver is appointed to take possession of additional property, such as personal property not subject to the secured lender’s lien, the fee owner may be entitled to compensation for the value of its use and possession.

After a receiver is appointed, and upon reasonable prior notice during normal business hours, a lender may enter and inspect real property that is being used as security to determine the extent of an actual or threatened release of hazardous substances. The lender may invoke this right of inspection only if the lender 1) has a reasonable belief of the existence of a past or present, actual or threatened, release of hazardous substances that was not disclosed to the lender in writing in connection with the banking, renewal, or modification of the loan, or 2) commences a judicial or nonjudicial foreclosure sale. If the lender’s inspection results in damage to the property, the lender must reimburse the borrower for costs.

As the real estate slump continues, more and more lenders face commercial borrowers who default on their mortgages. Many banks choose not to file a notice of default and take possession of property because they are reluctant to show another nonperforming loan on their balance sheet. They also are hoping that the real estate market will improve, even though most commentators proclaim that the real estate downturn is far from over. While the real estate industry continues to change dramatically and relentlessly, real estate practitioners should become well positioned to assist borrowers and lenders when the time comes to decide whether or not to appoint a receiver.
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5. See Barclay’s Bank of Cal. v. Superior Court, 69 Cal. App. 3d 593, 599, 600 (1977) (The court did not appoint a receiver because the mortgage terms did not include the right to collect rents and profits;); see also Hibernia Sav. & Loan Soc’y v. Belcher, 4 Cal. 2d 268, 271 (1935) (The court did not appoint a receiver because the parties failed to prove that the security was insufficient to satisfy the secured obligations.).
6. Code Civ. Proc. §568; Cal. R. Ct. 3.1179(a); Cal. R. Ct. 3d, Receivers §66.
7. See Nuclaid Farmers Ass’n v. LaTore, 252 Cal. App. 2d 768, 791 (1967).
8. Morand v. Superior Court, 38 Cal. App. 3d 347 (1974). In Morand, the appointment order authorized the receiver to file suit against one party. The receiver filed the suit and named other parties. The court held that the receiver had no authority to bring an action against other defendants because the receiver’s action was neither authorized by statute or by court order.
11. Any natural person is qualified to act as a receiver, except for a party to an action, an attorney representing any of the litigants, or a person interested in the action or related to the judge (unless the relatives obtain written consent from the clerk). Corporations cannot serve as receivers unless they obtain a certificate of authority from the Commission of Financial Institutions.
13. See Cal. R. Ct. 3.1180, which requires the receiver to obtain court approval prior to employing counsel and provides other specific requirements.
15. See Cal. R. Ct. 3.1179(b)(4); Hozz v. Varga, 166 Cal. App. 2d 539, 542 (1958) (The court confirmed that the receiver was authorized to expend funds to purchase furniture and make repairs because these acts were reasonably necessary for the conduct of its business.).
19. See Resolution Trust Corp. v. Bayside Developers, 43 F. 3d 1230 (9th Cir. 1994) (The receiver’s condominium sales were consistent with the developer’s intent to construct and sell the units.).
22. Id. at 275-76.
23. Resolution Trust Corp., 43 F. 3d 1230.
24. Id. at 1243.
25. Id.
27. 11 U.S.C. §543. The receiver may be excused from compliance with these duties if it can invoke any of the §543(d) exceptions.
30. Cal. R. Ct. 3.1179(b).
Holding On

Properly structured ERISA plans provide a powerful tool in asset protection planning

WHEN CONTEMPLATING A PLAN

for asset protection, practitioners and their clients often focus on the most exotic approaches, such as foreign and domestic trusts, transmutation agreements,1 and limited liability companies. Indeed, they often overlook the fundamentals of asset protection, including exempt assets—those that cannot be seized by creditors because they are exempt under federal or state law. Any asset protection plan should begin with an inventory of the client’s exempt assets, which should in turn lead to an inquiry whether the client’s nonexempt assets can be converted into exempt assets.

For debtors whose assets are in California, exempt assets offer powerful planning opportunities. Still, whether a particular asset is exempt from a creditor’s claims is often subject to a jumble of rules, exceptions to rules, and ambiguities. Practitioners seeking to address a client’s exposure to outstanding and potential claims must be aware of the applicable federal and state exemptions.2

Homestead Exemption. The best known but least effective exemption is the homestead exemption. At $50,000 for a single person, $75,000 for a married couple, and $150,000 for a homeowner 65 years or older or disabled,3 the California homestead exemption is simply not large enough to shield most Southern California residences from seizure, even in the current economic climate. As a result, homeowners often engage in “equity stripping”—loading their residences with debt up to the homestead amount. For example, a married couple who are subject to claims by creditors and who own a home with a fair market value of $500,000 might encumber the residence up to $425,000, on the assumption that the $75,000 homestead exemption will deter a creditor by making the residence worthless to any purchaser in a foreclosure sale. But equity stripping will deter only the most impatient creditor. A creditor who can wait will record the judgment in the county in which the residence is located, at which point the judgment will become a lien on the residence.

The homestead exemption might deter the creditor today or until next year, but with every passing year the homeowner’s equity will increase, either from natural appreciation or from the reduction in the principal. In the interim, the debtor cannot sell, refinance, or even devise the residence to an heir without first retiring the judgment. What is worse, the

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judgment will bear interest while the debtor will effectively make mortgage payments for the creditor. Neither the homestead exemption nor equity stripping will work to protect a debtor’s house from a creditor willing to bide its time.

Qualified Retirement Plans. If the homestead exemption is the weakest statutory exemption, then the most powerful exemption is the Employee Retirement Income Security Act of 1974 (ERISA). Protection of the liquid assets in a pension, profit-sharing, or 401(k) plan. For a plan to be qualified and enjoy substantial tax benefits as a result, the plan must contain an antialienation clause that prohibits the involuntary assignment or transfer of plan benefits to anyone other than the plan participant. The exemption is absolute, covering contributions to the plan made by both the employee and the employer—and applies even if the debtor is in control of the plan and has the ability to make immediate distributions from the plan.

Most significantly, because the antialienation requirement is a creature of federal statute, it will trump any state statute prohibiting fraudulent transfers.

Does this mean that an individual may cavalierly transfer assets into a qualified plan with the actual intent to “hinder, delay or defraud” a creditor and thereby shield the transferred assets from his or her creditors? In most cases, the answer is yes.

Those searching for exceptions to ERISA’s general rule permitting a debtor to transfer assets into a qualified plan and thus place those assets out of the reach of creditors will not find very many. One involves ERISA itself, which provides an exception for a divorcing spouse. It authorizes a court to issue a Qualified Domestic Relations Order (QDRO) directed at the plan administrator to facilitate an award for spousal maintenance, child support, or the division of property. As a result, qualified plan assets may become subject to division between divorcing spouses to the same extent as other marital assets.

Another implicates the U.S. Constitution’s supremacy clause. While the supremacy clause enables an ERISA antialienation clause to trump any state creditor’s claim, the supremacy clause does not do the same for federal claimants. Thus, the Federal Debt Collection Procedure Act takes precedence over an antialienation clause. For example, nothing in ERISA prevents the IRS from seizing a taxpayer’s interest in a qualified plan to collect federal income taxes. Nevertheless, the IRS has ruled that while it may levy upon the ERISA account of a plan participant, the plan administrator need not respond to the levy until the participant has a right, under the plan, to receive distributions. However, if the participant has a right to elect immediate distributions, the IRS may seize the participant’s account, even if the participant has not made such an election. Further, while the supremacy clause may not bar the IRS from seizing the ERISA account of a taxpayer, it will bar the Franchise Tax Board—or any other state tax collector—from doing so.

The principal exception to the general rule prohibiting the alienation of ERISA plan accounts applies to “owner only” plans, which are qualified plans whose only participants are the owners of a business (and their spouses). In a typical example of these plans, a doctor forms his or her own personal corporation, which establishes a qualified pension or profit-sharing plan with the doctor as the only participant in the plan.

The IRS and the U.S. Department of Labor together administer ERISA. A plan having only owner-participants will not disqualify the plan for tax purposes. The company will be free to make contributions to the plan on the sole owner’s behalf and obtain immediate tax deductions when doing so. But the Labor Department has long taken the position that ERISA exists to protect common law employees, and thus a plan whose only participants are owners and their spouses is not an ERISA plan. Accordingly, the antialienation protection of ERISA does not apply to owner-only plans. Moreover, courts have consistently upheld the Labor Department’s position. However, if the plan has just one nonowner participant, then the plan is fully qualified, and all participants, including the owners and their spouses, are fully shielded by the antialienation provision.

If the plan had common law participants when the contributions were made but no longer does—a fairly typical situation—the Labor Department’s position may have grave consequences. Whether the owner of the corporation discontinued the plan or terminated the corporation’s employees, it appears that any plan without nonowner participants is unprotected, regardless of whether the plan once had common law employees. If the doctor who formed a one-person corporation wants to assure that the plan assets are protected, the doctor simply needs to hire one common law employee and enroll that employee in the plan.

For those who do not have a qualified plan, the planning opportunity is obvious create one. There is nothing that prevents a per-
MCLE Test No. 187

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. The amount of the California homestead exemption varies according to the length of time the debtor has lived in the residence.
   True. False.

2. The amount of the California homestead exemption varies according to the debtor’s age.
   True. False.

3. If the IRS seeks the seizure of a California residence for unpaid federal taxes, the residence still qualifies for the homestead exemption.
   True. False.

4. Assets in a qualified retirement plan governed by ERISA are exempt from a claim by the Franchise Tax Board for state income taxes.
   True. False.

5. A divorcing spouse may make a claim on the contributions of his or her spouse to the spouse’s qualified retirement plan.
   True. False.

6. Assets in a qualified plan are exempt from creditors’ claims, regardless of the number of participants in the plan.
   True. False.

7. The IRS has elected not to seize assets in a qualified ERISA plan prior to the debtor-participant’s right to receive distributions, despite the power of the IRS to do so.
   True. False.

8. A state fraudulent conveyance statute will trump the antiantiélection provisions of ERISA.
   True. False.

9. The intentional overfunding of an ERISA qualified plan may result in the assets of the plan being seized by creditors.
   True. False.

10. ERISA affords no asset protection benefits after plan assets have been distributed to a plan participant.
    True. False.

11. A life insurance contract is an exempt asset under California law.
    True. False.

12. No portion of the cash surrender value (or loan value) of a life insurance contract is exempt from the claims of creditors.
    True. False.

13. An annuity contract generally is not exempt from creditors’ claims.
    True. False.

14. Receiving loans from a California private retirement plan will destroy the exempt status of the plan.
    True. False.

15. A California private retirement plan must have nonowner participants for the plan assets to be exempt from creditors.
    True. False.

16. ERISA governs an individual retirement account.
    True. False.

17. The loan value of an unmatured life insurance contract is exempt from execution.
    True. False.

18. Debtors whose IRAs contain more funds than necessary for their retirement needs will find their IRAs less likely to be exempt from the claims of creditors.
    True. False.

19. The recipients of the death benefits of a life insurance contract enjoy a limited exemption following the death of the insured.
    True. False.

20. An irrevocable life insurance trust (ILIT) may offer asset protection as well as estate tax reduction benefits.
    True. False.
son, even one facing an adverse judgment, from creating a qualified plan and transferring large sums of otherwise nonexempt assets into the plan, thus shielding those assets from creditors—provided that the plan has at least one nonowner participant. The annual amount that an employer may contribute to a qualified pension plan is based on factors such as the participant’s age and the amount

IRAs are exempt “only to the extent necessary to provide for the support of the judgment debtor when the judgment debtor retires and for the support of the spouse and dependents of the judgment debtor, taking into account all resources that are likely to be available for the support of the judgment debtor when the judgment debtor retires.”

The inquiry as to whether an IRA is
demanded necessary (by the plan’s actuaries) to fund the retirement benefit prescribed by the plan. For someone who is old enough, the amount that he or she can shield from creditors is substantial. A person who does control a qualified plan might be tempted to stuff assets into the plan in excess of the deductible amounts prescribed by the plan. This strategy is not advisable. For one, a contribution not permitted by the plan may be deemed to be void ab initio, resulting in it not being subject to the antialienation clause. What is worse, any excess contribution willfully made by an owner-employee will result in all plan contributions by the owner-employee being deemed distributed. Once distributed, they are not protected.

There is one last, but critical, limitation to retirement plans that afford many of the same federal law protection as ERISA plans. Hence do not provide the participant with the same federal law protection as ERISA plans.

The IRS has ruled that while it may levy upon the ERISA account of a plan participant, the plan administrator need not respond to the levy until the participant has a right, under the plan, to receive distributions.

Can the IRA holder replace the funds if the IRA is forfeited to a creditor? Thus, in one case, a court allowed a 60-year-old in poor health and facing the possibility of being laid off from work to keep a $167,000 IRA despite a $120,000 salary.

However, in another case, a 55-year-old working physician with no dependents and $5,000 in monthly income from an ERISA plan and Social Security could not keep a $270,000 IRA account. The inquiry as to whether an IRA account is “necessary” for retirement is determined by two criteria:

1. Is there a present need for the funds?
2. Is the IRA account necessary to fund the retirement benefit prescribed by the plan?

It is clear, however, that the exemption is designed to permit the individual to keep body and soul together upon reaching retirement; it is not intended to permit a retiree to maintain the lifestyle he or she enjoyed prior to retirement. Whether, and to what extent, an IRA account is “necessary” for retirement is determined by two criteria:

1. Is there a present need for the funds?
2. Is the IRA account necessary to fund the retirement benefit prescribed by the plan?

Thus, in one case, a court allowed a 60-year-old in poor health and facing the possibility of being laid off from work to keep a $167,000 IRA despite a $120,000 salary. However, in another case, a 55-year-old working physician with no dependents and $5,000 in monthly income from an ERISA plan and Social Security could not keep a $270,000 IRA account. Since one of the criteria is whether the individual will be able to replace the IRA, it appears that the key factor is the person’s age. It is highly unlikely that someone in his or her thirties could rely on the exemption.

IRAs are superior to ERISA plans in one respect: While ERISA protects the account only while the funds are in the plan, an IRA is protected even after the funds have been distributed, provided that the IRA owner can trace the funds to the IRA account.

Private Retirement Plans. To complicate matters further, California provides an unlimited exemption for “private retirement plans.” Under Code of Civil Procedure Section 704.115(b), “all amounts held, controlled, or in the process of distribution by a private
retirement plan, for the payment of benefits as an annuity, pension, retirement, allowance, disability payment or death benefit are exempt."

The problem is that the statute does not define a “private retirement plan.” Fortunately, the courts have filled in some of the blanks.

Clearly, a “private retirement plan” is not a plan governed by ERISA. However, a private retirement plan must arise in an employment context; someone cannot simply throw a bundle of otherwise attachable cash into an account labeled “private retirement plan” and hope that the cash will be exempt. The plan must be in writing and designed and used “principally” for retirement purposes. The statute permits loans to participants, provided that the loans are made in accordance with the plan’s procedures, evidenced by promissory notes, and charge a market rate of interest.

A California private retirement plan does not suffer from some of ERISA’s limitations. For one, the plan is not required to have at least one nonowner participant. Thus, an ERISA pension plan that fails due to the fact that it has only owner-participants may be saved—in its entirety—as a California private retirement plan. It is unlikely, however, that an ERISA profit-sharing plan would qualify as a private retirement plan unless the plan prohibited distributions prior to retirement.

Second, a private retirement plan is not subject to ERISA’s funding limitations. The plan participant can place any amount in a private retirement plan as long as the plan arises in an employment context and is designed and used principally for retirement.

The Ninth Circuit recently shed considerable light on the metes and bounds of a private retirement plan. In In re Rucker, the court held that the exemption would survive even if one of the plan owner’s motives was asset protection, provided that the owner could also prove that retirement planning was the principal object in creating the plan. Moreover, all the “facts and circumstances” would determine which was the predominant motive.

In Rucker, the private retirement plan was a failed ERISA plan because the debtor was the sole participant of the plan. Even worse, the debtor had intentionally over-funded the ERISA plan and apparently had filed fraudulent reports with the IRS. All the facts and circumstances militated in favor of a finding that asset protection—not retirement planning—was the principal object for the plan. Since all the facts and circumstances must be considered, the fact that no withdrawals or loans had been made from the plan was not a safe harbor. Conversely, if withdrawals or loans are made, it is not fatal to the exemption.

The lesson of Rucker is the same one that asset protection planners preach with respect to all forms of asset protection: The earlier the
A plan is created vis-à-vis the making of the claims against the owner, the more likely that the plan will survive scrutiny. Otherwise, the contributions will appear to be made merely to protect assets and not for retirement purposes as required.

While ERISA affords no protection once plan assets are distributed from an IRA or a private retirement plan, California does preserve the exempt nature of distributed assets, provided they can be traced to their exempt source.27 Assets from a fully exempt private retirement plan (or ERISA plan) that are rolled over into an IRA remain fully exempt and not subject to the IRA’s “necessary for retirement” limitation, according to the court in McMullen v. Haycock.28 As a result, counsel must now determine the provenance of the IRA. If it began its life as a qualified plan or a private retirement plan, it is fully exempt. If it has always been an IRA, the exemption is qualified.

A private retirement plan can be a powerful asset protection tool, provided that the owner is willing to part company with the contributed assets until retirement. Like the decision to transfer funds to a qualified plan, if the choice is losing the asset to a creditor now or waiting until retirement to enjoy the asset, most will choose the latter.

Life Insurance. Whatever planning that is done with life insurance is usually done with a view toward reducing estate taxes, not keeping assets exempt from the claims of creditors. The principal estate planning tool is the irrevocable life insurance trust (ILIT), a device that removes the death benefit of life insurance from the estate of the insured (and the insured’s spouse) at a relatively low gift tax cost. If the ILIT is established to remove the insurance from the taxable estate, the owner of the policy may not be the trustee of the ILIT or otherwise retain any incidents of ownership over the policy. If the ILIT is established early enough (before creditors assert their claims), the attributes inherent in every ILIT will likely shield the life insurance policy, as well as the policy proceeds, from creditors.

Aside from ILITs, California generally exempts life insurance from creditors. Under Code of Civil Procedure Section 704.100(a), “[u]nmatured life insurance policies (including endowment and annuity policies) but not the loan value of such policies, are exempt without making a claim.” A cursory reading of this statute leads to the conclusion that life insurance policies, endowment policies, and annuities are all exempt. But courts have ruled that to qualify for the exemption, the life insurance contract must be one that creates an estate in favor of the insured upon the insured’s death. This is the classic term or whole life policy that features a
Thus, if a person takes a large sum of otherwise nonexempt cash and uses it to purchase an annuity contract that provides for the payment of regular annuity payments over that person’s lifetime, the annuity payments will not be exempt.

As the code section makes clear, the insurance policies are exempt, but the “loan value”—that is, the cash surrender value—is not. Nevertheless, California makes it almost impossible for a creditor to access the loan value. By statute, the loan value of an unmatured life insurance contract is exempt from execution. If execution is not available, a creditor trying to seize the loan value can perhaps move for a turnover order or an order requiring the policy holder to exercise his or her right to borrow on the policy. But if the policy has been transferred to the trustee of an ILIT, even these remedies are probably not available. Moreover, if the creditor has a money judgment, no procedure is available to assist the claimant in accessing the cash value.

The purchase of life insurance, and the transfer of the policies to a trustee under an ILIT, can be a powerful asset protection tool. For those willing to purchase a policy that provides for a death benefit—a classic life insurance policy—liquid assets that might have been easily attachable are suddenly free from the claims of creditors.

If the insured dies, and the life insurance becomes cash, the insurance proceeds that are now in the hands of the beneficiaries remain exempt, but only to the extent “reasonably necessary” for the beneficiaries’ support. If the cash had not been used to purchase life insurance, the decedent’s creditors could have proceeded against the estate. But this fact provides little opportunity for planning. Most view dying as too aggressive an asset protection technique.
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Los Angeles Lawyer December 2009 37
Can a Lawyer Ethically Agree with a Client to a Contingency Fee Which Is Based on a Percentage of the Combined Amount of Damages and Any Statutory Fees Awarded?

**SUMMARY:** This Opinion addresses whether it is permissible, in a contingency representation, for the attorney and client to include within the gross recovery the statutory award of attorney’s fees which, absent an agreement to the contrary, would otherwise belong to the attorney. The issue is whether such an agreement that allocates the gross recovery between the attorney and the client constitutes “fee splitting” with a nonlawyer. The Committee believes that it does not.


**FACTS**

Attorney represents Client, a nonattorney, as the plaintiff in an employment discrimination case brought in state court under the California Fair Employment and Housing Act (California Government Code §§12900 et seq.) (FEHA). If Client prevails on her FEHA claim, the court may, in its discretion, award reasonable attorney’s fees to the plaintiff’s attorney. (California Government Code §12965(b))

Attorney is representing Client pursuant to an otherwise valid written retainer agreement entered into at the beginning of the retention. The retainer agreement provides, inter alia, that Attorney shall be entitled to ¼ of any gross recovery from the litigation. Gross recovery is defined in the agreement as all recovery for the client, including any court-awarded attorney’s fees and costs. The remaining ¼ of the gross recovery belongs to Client.

**ISSUE**

Can an attorney and a client ethically agree to divide the gross recovery in a contingency case that includes the amount of a statutory award of attorney’s fees? Does such an agreement violate Rule of Professional Conduct 1-320, subdivision (a)?

**ANALYSIS**

Contingency fee agreements must be in writing and must include a “statement as to how disbursements and costs incurred in connection with the prosecution or settlement of the claim will affect the contingency fee and the client’s recovery.” (California Business and Professions Code §6147(a)(2))

Rule 1-320(A) of the California Rules of Professional Conduct provides, subject to enumerated exceptions, that “neither a member nor a law firm shall directly or indirectly share legal fees with a person who is not a lawyer…” In Flannery v. Prentice, 26 Cal. 4th 572, 575, 590 (2001) (Flannery), the California Supreme Court held that, absent an agreement to the contrary, a statutory award of attorney’s fees under FEHA (California Government Code §12965) belongs to the attorney, not the client.2 In doing so, the Court held:

For the foregoing reasons, we conclude that attorney fees awarded pursuant to section 12965 (exceeding fees already paid) belong, absent an enforceable agreement to the contrary, to the attorneys who labored to earn them. The preceding analysis, of course, may not be dispositive—indeed, will not even come into play—where the parties have made an enforceable agreement disposing of an award’s proceeds. Whether an enforceable agreement exists, or what its terms may be in any given case, are of course questions of fact. (Id. at 590, italics added)

Flannery discussed, but did not explicitly decide, the issue of whether sharing a statutory award of attorney’s fees with a client would run afoul of Rule 1-320(A)’s prohibition upon “fee splitting.” (Flannery, supra, 26 Cal. 4th at 586-87 and fn. 15) Nonetheless, the italicized language from Flannery can be read as suggesting that it is appropriate for the attorney and client to agree, in an otherwise enforceable retainer agreement, to divide the statutory award of attorney’s fees that could otherwise belong to the attorney. Indeed, Flannery assumed that the parties would contract for a disposition of the statutory attorney’s fees. (Id. at 588, fn. 16) Under the facts of this Opinion, attorney and client have agreed to divide percentages of the recovery inclusive of both the client’s award and the fee award, and would properly be viewed not as fee split-
The Committee believes that permitting such contractual agreements does not implicate the policies against “fee splitting.” In Opinion No. 510, this Committee opined that the “rationale behind [Rule 1-320(A)] and its intended application are, primarily, to protect the integrity of the attorney-client relationship, to prevent control over the services rendered by attorneys from being shifted to lay persons, and to ensure that the best interests of the client remain paramount.” (See also McIntosh v. Mills, 121 Cal. App. 4th 333, 345 (2004), discussing policy reasons for prohibiting “fee splitting” with nonlawyers. McIntosh did not address the division of a court-awarded fee with the client.) In Opinion No. 447, the Committee opined that it was permissible for a statutory award of attorney’s fees to be used to reduce the amount of the contingency fee. In doing so, the Committee opined that the policies against “fee splitting” are not implicated “if the lay person is a client who has employed the Attorney under a prior specified contingency fee agreement…” In Opinion No. 515, the Committee opined that it would not constitute “fee splitting” for a retainer agreement to provide for a cap on hourly fees and for any statutory award of attorney’s fees to be reimbursed to the client, once the law firm had been paid its full hourly rate. Lastly, the negotiation of the initial retainer agreement between an attorney and client is generally considered an arm’s-length transaction by which the attorney and client come to an agreement regarding the payment of fees. Except for certain situations where fees

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Recently, a pro bono attorney helped a man from El Salvador who was placed in immigration court proceedings because he was told by a “notario” that it would be easier for him to get a “green card” before the Immigration Judge. Besides giving bad legal advice and practicing law without a license, the notary did not know that this person was eligible for special relief known as NACARA. The volunteer attorney, working with the Immigration Court, helped this person stay in the United States by filing the correct paperwork so he could obtain his “lawful residency status” (green card). This is just an example of the type of cases you will see and the people you will be helping as a pro bono attorney.

The Panel operates on Wednesdays and Fridays, when pro bono attorneys show up at designated courtrooms for Master Calendar hearings only. Volunteer attorneys are then matched with participating Respondents. A special room has been set aside on the 14th floor of the Immigration Court so volunteer attorneys and Respondents can speak confidentially. Once Respondents are given counsel and advice they then proceed with the attorney back to the Immigration Judge to plead their case.

Each participating attorney will be asked to do one master calendar hearing per month, or what your schedule will allow. The Panel coordinator will try to be as flexible as possible.

IF YOU WOULD LIKE TO PARTICIPATE, PLEASE JOIN US FOR A TRAINING ON JANUARY 27, 2010.

Remember Pro bono representation is only for the first master calendar appearance. Immigration Court experience is preferred, but not necessary.

For further information, go to www.lacba.org/showpage.cfm?pageid=1758 or you may call Mary Mucha, Project Director, at 213-485-1873.
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PERSONAL INJURY CASES ACCEPTED ON LIEN BASIS
Nuts & Bolts: Prejudgment Remedies

ON SATURDAY, DECEMBER 5, the Remedies Section will present a program on prejudgment remedies—a means by which creditors can preserve the value of their interest by preventing debtors from transferring, encumbering, dissipating, or concealing assets. Speakers Alan J. Cohen, Mark L. Share, Susan L. Vaage, and A. David Youssefyan will cover the nuts and bolts of prejudgment writs of attachment and possession and give an overview of receiverships. The program materials will include sample motions and forms that can be used for future cases. The program will take place at the Los Angeles County Bar Association, 1055 West 7th Street, 27th floor, Downtown. Before 8:30 a.m., parking at 1055 West 7th Street costs $6; after 8:30 a.m. but before 5 p.m. it costs $10 with LACBA validation. Additional parking is available in surrounding lots for $5 to $7. On-site registration will begin at 8:30 a.m., with the program continuing from 9 a.m. to 12:30 p.m. The registration code number is 010653. The prices below include the meal.

$50—CLE+Plus members
$75—Remedies Law Section members
$90—LACBA members
$125—all others
3.25 CLE hours

Unfair Competition Law and Employer-Employee Relations

ON TUESDAY, DECEMBER 8, the Antitrust and Unfair Business Practices Section will host a program featuring speakers Daniel M. Flores, Dan Forman, and Cheryl D. Orr, who will address the questions that California companies typically have about the legality and enforceability of employee covenants not to compete, nondisclosure agreements, predatory hiring, and other similar issues at the intersection of employment law and unfair competition law.

In addition, the section is pleased to offer an opportunity for attendees of this program to network professionally with section members and law practitioners, from both sides of the bar, the bench, and the expert witness box. The networking gathering will be held just prior to the program, from 11:45 a.m. to 12:15 p.m., at the Los Angeles County Bar Association, 1055 West 7th Street, 27th floor, Downtown. Before 8:30 a.m., parking at 1055 West 7th Street costs $6; after 8:30 a.m. but before 5 p.m. it costs $10 with LACBA validation. Additional parking is available in surrounding lots for $5 to $7. On-site registration and a meal will be available at 11:30 a.m., with the program continuing from 12:30 to 1:30 p.m. The registration code number is 010703. The prices below include the meal.

$15—CLE+Plus members
$35—government attorney LACBA members
$45—Antitrust and Unfair Business Practices Law Section members
$65—LACBA members
$70—all others
1 CLE hour

ABCs of SNDAs

ON WEDNESDAY, JANUARY 6, the Real Property Section and the General Real Property Subsection will host a program on the purpose of an Snda, how it is enforced, and consequences that may arise if one is not in place at the time of a property foreclosure. The lecture will focus on terms that every tenant should negotiate into an Snda and terms most lenders cannot (and should not) go without.

This event may be attended in person or online as a Webinar. Early Webinar registration is required. Log-in information will be forwarded to each Webinar registrant 24 hours before the event, so please ensure that you provide your correct e-mail address. To receive full CLE credit for viewing the Webinar, registrants must log in individually, and it is recommended that registrants log in 5 minutes early. The program will take place at the Los Angeles County Bar Association, 1055 West 7th Street, 27th floor, Downtown. Before 8:30 a.m., parking at 1055 West 7th Street costs $6; after 8:30 a.m. but before 5 p.m. it costs $10 with LACBA validation. Additional parking is available in surrounding lots for $5 to $7. On-site registration will be available starting at noon, with the program continuing from 12:30 p.m. to 1:30 p.m. The registration code number is 010657.

$20—CLE+Plus members (with meal)
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The Los Angeles County Bar Association is a State Bar of California MCLE approved provider. To register for the programs listed on this page, please call the Member Service Department at (213) 896-6560 or visit the Association Web site at http://calendar.lacba.org/where you will find a full listing of this month’s Association programs.
The Danger of “Anti-Libel Tourism” Legislation in America

AN EXTRAORDINARY TURN OF EVENTS in federal and state legislatures in America severely affects the rights of those aggrieved in libel matters. The legislatures of New York, Illinois, and Florida have enacted statutes under the theory that they are preventing “libel tourism.” In New York, the law is more ominously titled the Libel Terrorism Protection Act. A similar bill, HR 6146, is pending in the U.S. Congress. Now California has joined the ranks. On October 11, 2009, the governor signed Senate Bill 320 into law. These laws nullify the enforcement in the United States of legitimate court judgments abroad if they do not meet the free speech protections guaranteed under the First Amendment of the U.S. Constitution. Some of the legislation introduced in Congress would go so far as to award damages to Americans sued for libel overseas.

The inspiration for these laws comes from American writer Rachel Ehrenfeld, who lost by default a libel case brought against her in England by Saudi Arabian businessman Khalid bin Mahfouz. The case against Ehrenfeld centered on her book Funding Evil: How Terrorism Is Financed—and How to Stop It, in which she accused bin Mahfouz of funding terrorism. Rather than defending herself in the English court, Ehrenfeld filed a preemptive lawsuit in New York in an attempt to get a declaration that the judgment made by the English High Court of Justice should not be enforced in the United States because, according to U.S. defamation law, her book did not make her guilty of libel. The New York court, however, rejected her suit because it did not have personal jurisdiction over bin Mahfouz.

After Ehrenfeld’s losses in the English and New York courts, she began campaigning for the so-called libel tourism laws. In the four states where she has succeeded, the existing statutes regarding the enforcement of foreign judgments of libel have been amended to make them unenforceable unless the American court first determines that the defamation law applied in the foreign court’s adjudication provided “at least as much protection for freedom of speech and press...as would be provided by the United States Constitution and the State Constitution.” In effect, these laws call for foreign legal systems to abide by the First Amendment of the U.S. Constitution.

A Shift in the Burden of Proof
In practice, these statutes shift the burden of proof regarding the truthfulness of statements from the defendant to the plaintiff. Ehrenfeld never showed proof of the truth of anything she wrote about bin Mahfouz in her book, yet “Rachel’s law” forces the “American rule” of proof on foreign courts. This may actually encourage libels outside the United States if the perpetrator knows the difficulty the person libeled will have in proving falsity, either abroad or in the United States.

The scenario becomes more complicated if the libel concerns a matter of public interest or involves a public figure. In the United States, such plaintiffs must show “constitutional malice”—that the journalist acted in reckless disregard (had “substantial doubts” about the statement’s truth or falsity) or intentionally. Thus, well-known celebrities such as Britney Spears and Jennifer Lopez, who have brought libel actions in foreign courts, would have to return to the United States to reprove their cases.

Courts in the United Kingdom have the same respect for free speech as those in the United States but place a much greater emphasis on ensuring that the speech is fair and accurate. Although U.K. courts do give more protection for public figures than in the United States, this is balanced by the “public interest defence,” which was invoked in a recent landmark decision in the House of Lords. This defense is analogous to the “constitutional malice” requirement set forth by the U.S. Supreme Court in New York Times v. Sullivan. One reason U.K. courts give more protection to public figures than does U.S. law is that they place more emphasis on the value of one’s reputation, the bedrock value upon which all libel law has been built worldwide and which, though given lip service as a balancing-test component by U.S. courts, has been eroded by deference to free speech arguments advanced by the media.

Ehrenfeld has been able to make such a strong showing because of the strength of her media backing, which is effectively and self-interestedly pursuing these laws, and because there is no organized opposition to them. The public figures and celebrities who will be most affected are generally unaware these laws are being enacted—and those who have yet to be libeled do not have their antennae up. Unless more voices, particularly from abroad, are raised against the passage of these laws, we can expect more to be passed in coming years.

BY NEVILLE L. JOHNSON, JOHN J. WALSH, AND W. PAUL TWEED

Neville L. Johnson is a partner in the Beverly Hills firm of Johnson & Johnson LLP, where he specializes in media law. John J. Walsh is with Carter Ledyard & Milburn LLP, a New York firm, where he represents plaintiffs in libel and other media matters. W. Paul Tweed is a solicitor at the U.K. firm of Johnson Solicitors who represents libel claimants. Kendall Bass, a student intern, assisted in writing this article.
August 4, 2009

John R. “Jack” Trimarco
9454 Wilshire Blvd., 6th Floor
Beverly Hills, CA 90212

Dear Jack,

I am writing this letter with my deepest thanks for your tremendous efforts in assisting in a murder investigation which focused on my client, Damien Gatewood.

During the early morning hours, shots were fired at a house party in the Southern California area. Tragically, a guest was struck and died. Questionable eye witness identification by one neighbor, identified Damien Gatewood as the shooter.

Mr. Gatewood was arrested days later and had been incarcerated at Wayside Honor Ranch for one year awaiting trial.

I never believed that the authorities had the right man. Your long recognized and unmatched expertise in the polygraph field made you the obvious best choice to perform this critical examination.

You contacted me after you examined Mr. Gatewood. You told me that according to your examination Mr. Gatewood was conclusively not the shooter, a fact which was supported by retired FBI Agent and polygraph examiner Ron Homer, during his quality control.

Armed with the Examination video, polygraph report and your curriculum vitae, I met with the prosecutor assigned to the case. He directed me to the Los Angeles County Sheriff’s Department Polygraph Unit. I met with them to evaluate your test. They all acknowledged your unimpeachable integrity and expertise. They reviewed all charts, documents and video. I was advised by the Unit Chief that you ran a perfect examination and they agreed that Mr. Gatewood was not the shooter. Two days later the case was dismissed and an innocent man was not convicted.

It is a tribute to your reputation that polygraph testing conducted by you is so well received and respected in the legal community.

Warm Regards,

MARKS & BROOKLIER, LLP

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