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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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Finding a Safe Harbor Mentor

A PERFECT STORM OCCURRED in October 1991 when three storms combined into one off the coast of Gloucester, Massachusetts. The combined storm created waves 10 stories high and winds of 120 miles an hour, whipping the sea to heights that only a few witnessed and fewer survived. While the perfect storm, as memorialized in a book and recounted in cinema, was a historic event, it can be compared to events that happen in everyday lives in the workplace. When opposing counsel appear inflexible, clients overly demanding, supervisors watching and evaluating every move, and colleagues circling like vultures waiting for the untutored to stumble and fail, the legal profession can seem like the perfect storm. To stave off the potential devastation of a perfect legal storm, it is important to find a mentor who can act as a safe harbor, assisting in navigating through the politically stormy waters of the legal profession.

A safe harbor mentor serves as a trusted counselor or teacher—someone to whom the protégé can ask questions, seek guidance, bounce ideas, and discuss issues one would not normally discuss with a supervisor. Providing a safe harbor, however, is not to be confused with harboring misconduct. Mutual trust in a safe harbor relationship is essential. A safe harbor mentor should also not be put in an advocacy or mediator role between the protégé and his or her supervisor. Instead, a safe harbor mentor guides the mentee in making sound professional decisions.

A mentor can be assigned, but a safe harbor relationship is more likely developed with time and familiarity. Whether the mentor is a former employer or more experienced colleague, effective mentors often counsel and guide behind the scenes. Mentors who formally contribute to the administrative performance process may not be able to function as a true safe harbor because the dual function of mentor and evaluator may defeat the purpose of a safe harbor. A mentor also need not be publicly identified and may be in a better position to facilitate introductions likely to lead to networking and other professional opportunities by functioning behind the scenes.

Building Desirable Protégé Traits

Supporting a protégé’s professional endeavors reflects on the mentor as well as the mentee. Therefore, it behooves the protégé to build traits that make one attractive to a prospective mentor. First, a desirable mentee is responsive, prompt, and organized. It is true that first impressions are lasting. There is nothing more frustrating or off-putting than calling a protégé and not receiving a response, or receiving a delayed response with no plausible excuse. A desirable protégé is also one who is self-motivated, disciplined, and willing to take action. While a protégé is not obligated to act on the mentor’s advice, demonstrating that the advice had a meaningful impact on the protégé’s decision encourages the mentor to continue providing a safe harbor.

A desirable protégé has a strong work ethic and demonstrates internal motivation, which can come from developing a benchmark of productivity. This benchmark creates a buffer in a cutthroat competitive environment. Insecure competitors build themselves up by tearing others down, but this type of competition is limiting because one only rises as high as the other falls. Keeping an internal benchmark allows the protégé to rise as high as his or her capability dictates.

A desirable protégé knows how to maintain inner peace and employs a strategy for dealing with stress, which is part of the legal profession. It is easy to bury stress in negative relievers such as excessive alcohol consumption and abuse of drugs (prescription or otherwise). Legal implications aside, abusing alcohol and other drugs places one’s law practice at risk because it negatively affects professional performance and can discourage a potential safe harbor mentor.

A Safe Harbor Relationship

Most likely it will be incumbent on the protégé to recognize someone who can fulfill the need for a mentor. It is important to choose a mentor that the protégé knows and to whom the mentee feels comfortable expressing thoughts and fears, because open and candid communication is a key factor in developing a safe harbor relationship. Holding back information can inhibit a mentor from providing effective guidance.

Another factor in developing an effective safe harbor relationship is confidentiality. A safe harbor is effective if both parties are confident that conversations will remain confidential. Maintaining confidentiality allows for candid dialogue and allows the mentor to freely disclose professional and personal information without fear that confidences will be disseminated.

A third factor in developing a safe harbor relationship is keeping in contact with the mentor. This often means initiating contact and suggesting meetings. This allows the mentor to guide the protégé’s professional development and speak knowledgeably about the mentee to others. While there may be other important factors in developing a safe harbor relationship, the key is being flexible and adaptable and allowing the relationship to grow naturally. For the mentee who shows trustworthiness and respect, the benefits in developing a successful safe harbor relationship are immeasurable.

April A. Christine is an assistant U.S. attorney for the Central District of California, where she prosecutes gang-related violent federal crimes. She is vice president of the Barristers. The views expressed in this article are the personal views of the author, and do not in any way represent the views of the U.S. Department of Justice or the U.S. Attorney’s Office.
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AGENDA

MORNING
Breakfast Session: Tips for Success for Young Lawyers
- The Economy: Where it Has Been and Where it is Headed
- What Happens Next: The Economy and Real Estate
- Taking Advantage of Distress
- Climate Change and Land Use Regulation
- Important Leasing Issues in Today's Economy

AFTERNOON
Three Specialized Programming Tracks: Finance, Development, Strategies for Difficult Times
- Luncheon Keynote by Thomas J. Barrack, Jr.
- Sources of Equity
- Traffic and Southern California
- Bankruptcy, Workouts and Foreclosures
- Sources of Debt
- Green Building and Construction
- Updates on Fees, Tax Laws, High Speed Rail and Water Rights

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- Thomas J. Barrack, Jr., Colony Capital, LLC
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- Jonathan E. Klein, Fortress Investment Group
- The Honorable Quentin L. Kopp, California High-Speed Rail Authority
- Larry J. Kosmont, Kosmont Companies/Renaissance Community Fund
- M. Leanne Lachman, Lachman Associates, LLC
- Dr. Malcolm Lewis, Constructive Technologies Group (CTG), Inc.
- Vance G. Maddocks, CB Richard Ellis Investors
- Roy March, Eastdil Secured
- Dr. Glenn R. Mueller, Denver University, F.L Burns School of Real Estate & Construction Management
- Norman Radow, RADCO Development Solutions
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Section 363 Real Estate Sales Are Still Feasible after *Clear Channel*

**ONE ICON OF THE CURRENT REAL ESTATE** downturn is a partially or recently completed housing project with a defaulted senior construction loan and a fair market value lower than the amount of the liens. Sadly, as residential values continue to decline, many of these projects are not worth enough to pay even the remaining balance of the construction loan, much less the claims of junior lenders, unpaid subcontractors, and suppliers. The senior construction lender, the borrower, and the guarantors of the loan—together with any others holding any valuable interest in the project—are likely to want to get the project sold and converted into cash as quickly as possible, if only to protect their balance sheets from worse decline. If completion of construction is elected as a means of minimizing the loss, time is of the essence with real property collateral in a declining market.

Unfortunately, given the continuing drop in residential real estate values, it usually is too late for many of the junior lien stakeholders. In a downturn, what might have been at least partially secured liens become unsecured. Junior lien holders get no advantage from consenting to a sale that gives something to the construction lender and guarantors but leaves nothing to them. Their consent—or some other lien-cleansing procedure—will be required if marketable title is to be consensually conveyed to the prospective purchaser. Out-of-the-money junior creditors, thus, typically adopt holdout strategies when asked to consent to a sale, refusing to execute consensual lien releases unless they are paid. Even if the senior lender were inclined to cede some of the sale proceeds to the juniors to buy peace, identifying, organizing, and binding everyone to a consensual agreement can be a monumental task.

Nonjudicial foreclosure seems the obvious procedure to overcome an obdurate, out-of-the-money junior lienor (perhaps combined with a receivership funded by the construction lender to complete construction before foreclosure). Unfortunately, the nonjudicial foreclosure solution often is neither immediately available nor complete. Even if a foreclosure sale is completed before it is stayed by a state court injunction or the filing of a voluntary or involuntary bankruptcy petition, the successful bidder at the foreclosure sale may not buy free and clear of apparently junior lien claims if the junior lien claimants properly preserve claims that the construction lender’s deed of trust has suffered a partial or complete loss of priority.

Given these complexities, construction lenders and their counsel have recently looked upon borrower bankruptcies more favorably, in part because Section 363(f) of the Bankruptcy Code gives the debtor in possession or trustee in bankruptcy the power to sell its assets, for example a housing project, “free and clear of liens”—even over the objection of junior creditors—after notice and an opportunity to be heard is afforded to the interested parties. Until recently, this type of sale (commonly referred to as a 363 sale) was considered permissible over the objection of junior lienors either before plan confirmation or pursuant to a plan of reorganization by the majority of bankruptcy courts issuing reported decisions on the question. No reported appellate decision had thoroughly addressed the issue until late last year, when the Bankruptcy Appellate Panel (BAP) of the Ninth Circuit Court of Appeals handed down *Clear Channel Outdoor, Inc. v. Knupfer (In re PW, LLC).* That decision is now widely, and prematurely, cited for the proposition that a 363 sale free and clear of the lien of an objecting undersecured junior lien holder can only be accomplished pursuant to a plan of reorganization and not before.

The 363 sale typically involves an agreement between the debtor and a third-party cash purchaser and usually—although not always—involves an auction in which other prospective purchasers can outbid the initially identified buyer (sometimes referred to as the stalking horse). If the collateral is encumbered by a lien, the lien holder must be given an opportunity to bid, and if it is the successful bidder, the lien holder is authorized to offset the allowed amount of its claim against the purchase price. This credit-bid right protects the lender from having its collateral sold out from under its feet at a price below the lender’s perception of value. Aside from generating potential purchasers, the possibility of the 363 sale also creates a focal point for settlement among creditors and the debtor.

The objectives of each debtor vary, but some common ones are 1) generating unencumbered funds to pay the fees and costs of the trustee, the trustee’s counsel, and other administrative expenses, 2) generating unencumbered funds to pay trade creditors, 3) minimizing the deficiency that may be owed by the estate, by guarantors, or by other co-obligors, and 4) giving the debtor or affiliates of the debtor an opportunity to buy the collateral for a price greater than the lender’s perception of value. The lender’s objectives also vary but typically will focus on speed of resolution, avoidance of liability to third parties, obtaining clear title, and maximization of recovery—not only from the debtor but also from guarantors and other co-obligors.

Thus, the terms that the lender may concede in exchange for speed of resolution may include:

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**Aside from generating potential purchasers, the possibility of the 363 sale also creates a focal point for settlement among creditors and the debtor.**

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KENNETH N. RUSSAK is a shareholder in Frandzel Robins Bloom & Csato, L.C., in Los Angeles and practices bankruptcy, litigation, and commercial finance law.
• The lender agrees to set aside a specified dollar amount of the net sales proceeds—or to separately advance funds—to be used, perhaps, 1) to pay the debtor’s legal fees and other administrative expenses, 2) to secure the recovery of a junior creditor if it later proves the seniority of its lien, and 3) to pay some portion of the claims of the out-of-the-money junior claimants.

• The lender agrees to credit-bid no less than a minimum negotiated minimum price—to reduce deficiency obligations owed by the estate, by guarantors, or by other nondebtor co-obligors.

• The lender agrees to stop bidding at a negotiated maximum amount if a competing cash bidder outbids the cap.

The usual nonbankruptcy concerns about collusive bidding are obviated in bankruptcy, because the entire process is disclosed in advance to all parties in interest, expressly approved by the bankruptcy court, and typically conducted in a live auction in open court. Interested parties that were not invited to participate during the negotiation will have an opportunity to object to the 363 sale motion and thereby effectively demand a seat at the negotiating table. Once the parties agree to the bankruptcy and nonbankruptcy terms of the proposed transaction, they will seek approval from the bankruptcy court of not only the substance of the transaction but also the bid procedures.

As a substantive matter, even before the tests are considered, the debtor will be required to prove 1) there is a sound business reason for selling the asset, 2) the transaction is proposed in good faith, 3) notice of the sale has been adequate, and 4) the terms of the transaction are fair and reasonable. One of the key issues to be considered will be whether the value of the asset is increasing or declining. Sometimes the bid procedures are the subject of a separate motion, set for hearing before the motion to approve the sale. Parties can preview with the court matters such as the break-up fee and overbid amounts and readjust their deal if the court refuses to approve the procedures. Whether set for hearing at the same time or sequentially, all the elements of the sale will be subject to the approval of the court, after notice and an opportunity to be heard has been afforded to all parties in interest.

The auction is set concurrently with or shortly after the hearing on the motion for authority to sell free and clear of liens under Section 363, at which time the debtor in possession, trustee, or purchaser submits evidence of value, either in the form of appraisal evidence or by testimony as to efforts to sell the project and the results of those efforts. Assuming the bankruptcy court rules that the requirements for granting the motion have been met, the court will then call the auction. It is not uncommon for overbidders to appear and actively bid up the price, although in the current real estate market, where bottom feeding still seems to be more the rule than the exception in most parts of the country, debtors and lenders should not count on overbidding. At some point, however, a highest bid will be accepted and the court will approve the sale.

In addition to the general standards for a sale out of the ordinary course of business, when a debtor seeks to sell free and clear of liens pursuant to Section 363(f)(3), a focus on value of the property is mandatory, because a court can only authorize a sale over the objection of junior lien holders if it makes a finding that “the price at which such property is to be sold is greater than the aggregate value of all liens on such property.” In bankruptcy parlance, the aggregate value of the liens will be equal to the value of the collateral if the collateral is worth less than the aggregate amount of the claims secured by those liens. Those claims that have become partially or wholly unsecured will be treated as secured only to the extent of the value of the collateral available to the particular creditor, with the excess “deficiency” amounts being treated as unsecured claims.

The service of a properly drafted motion for an order authorizing a sale free and clear of liens will flush out any unasserted claims that the lender’s lien has suffered a loss of priority—whether the sale is a credit-bid or cash bid sale—because the sale motion will address whether and to what extent sale proceeds will be impounded with the liens transferred to the proceeds or paid to the senior lender. In a cash sale to a third-party purchaser, that protection usually comes in the form of an order impounding sufficient sales proceeds to stand as security for the trade creditor’s claim, should its loss of priority claim ultimately succeed. If the senior lender is the successful bidder, the court may require the senior lender to pay a sufficient portion of the purchase price in cash to be held as alternate security to protect the putative senior trade creditor, should it prevail in the lien priority dispute. Granted, the bankruptcy court will not adjudicate a lien priority dispute in the context of a 363 sale motion. The filing of an adversary complaint for declaratory relief is the proper procedure to seek a judicial resolution, if one cannot be negotiated; but the sale motion will at least identify potential lien claimants asserting priority and give the parties an opportunity to negotiate a resolution.

The holdout strategy may rear its head in this context, but the risks to the trade creditor holding a weak claim of priority are much greater in a bankruptcy proceeding, because the dispute is likely to be resolved much more quickly in a bankruptcy case than in a state court lawsuit. Even if the lender or debtor is forced to file a complaint for declaratory relief, in a declining market the bankruptcy court may order a very brisk pretrial calendar and consolidation of the adversary trial with the hearing on plan confirmation, because the lien priority dispute is likely to materially affect plan confirmation. When faced with the alternative of a relatively quick adjudication of a weak claim, the trade creditor may accept a compromised payment early in the case, rather than face a lender unwilling to make any concessions, if it is put to the burden of litigating the issue and the delay of a plan confirmation battle. The flip side of that coin, of course, is that the stronger the claim of loss of priority, the more likely the lender will be to make substantial concessions to the “junior” trade creditor, in order to manage the risk of losing at trial.

Even if negotiations to compromise the lien priority battle fail, the sale may nonetheless be approved, if adequate protection can be afforded to the trade creditor claiming priority by the posting of a fund to stand as alternate security for the alleged priming claim. The lender may not be willing to be the stalking horse in the 363 sale under those circumstances, but it is at least an available option. In the end, if the parties are unable to resolve the lien priority dispute, an adversary proceeding may be the only alternative (unless, of course, a title insurance company steps up and funds a settlement). The fundamental point is that the 363 sale motion, at a minimum, will identify and quantify the magnitude of lien priority risks much earlier than may otherwise occur and may accelerate resolution of disputed claims of priority.

As a result of these dynamics, before Clear Channel, the preplan 363 sale of a defaulted construction project emerged as an effective strategy to identify, organize, address, and deal with holdout, out-of-the-money junior creditors. The process results in the identification and management of junior lien claims seeking priority. If those claims are successfully managed, the process also results in the conveyance of title that has been blessed with the imprimatur of an order for sale free and clear of liens. The title conveyed by foreclosure should be the equivalent, but experience teaches that it often is not. If for no reason other than the limits of title insurance, the foreclosing lender may well be confronted with limits on its ability to convey insurable, marketable title. An order directing a sale free and clear of liens clearly is superior.

A Ninth Circuit Challenge

The growing popularity of preplan 363 sales of distressed real estate has been at least tem-
porarily derailed in the Ninth Circuit. *Clear Channel* holds that Section 363(f) did not permit the secured creditor in that case to credit bid its debt and purchase estate property free and clear of valid, nonconsenting junior liens outside of a plan of reorganization. The decision appears to hold that this type of sale, if it is to be authorized at all, is only proper if part of a plan of reorganization that has survived the time-consuming and expensive plan confirmation process. To the extent binding on or persuasive to other courts in the Ninth Circuit or elsewhere, *Clear Channel* would appear to raise a significant hurdle for lenders and borrowers seeking to use the 363 sale strategy to obtain a prompt resolution of a loan if the collateral is burdened by the claims of out-of-the-money junior creditors.

The hurdle, however, may not be as daunting as it may appear. The BAP first analyzed the 363 sale in *Clear Channel* under Section 363(f)(3), which authorizes a sale free and clear of liens if the “price at which such property is to be sold is greater than the aggregate value of all liens on such property” and found it wanting because the credit-bid price only equaled, but did not exceed, the value of its lien, because the lender’s credit-bid was the first and last bid at the auction. Embedded in this conclusion is the assumption—apparently urged by the parties in the proceedings before the bankruptcy court—that a credit price “paid” by a senior lender is the value equivalent of a cash price paid by a third-party purchaser. That is an assumption that warrants closer examination.

It can be taken as a given—and as a matter of definition—that the price paid by an all cash, third-party bidder at an open and fair auction sale is the fair market value of the collateral. The Appraisal Institute defines “market value” as “[t]he most probable price, as of a specified date, in cash, or in terms equivalent to cash, or in other precisely revealed terms, for which the specified property rights should sell after reasonable exposure in a competitive market under all conditions requisite to a fair sale, with the buyer and seller each acting prudently, knowledgeably, and for self-interest, and assuming that neither is under undue duress.” However, the conclusion that a credit-bid price is the dollar-for-dollar equivalent of such a cash bid glosses over two key components of the value definition: 1) cash equivalency and 2) lack of undue duress.

A lender holding an undersecured claim in a bankruptcy case is hardly a free actor regarding its investment decisions for the failed project. It has already disbursed money, typically in the millions of dollars, to make or acquire the loan. It does not have the luxury of freely deciding to take its investment dollars elsewhere. It made that decision long before and is now locked in a battle to get a return of as many of those dollars as possible. Whether it is a regulated lender such as a bank or insurance company or an unregulated lender managing its own or its investors’ funds, it will be under significant pressure to resolve its problem loans promptly and efficiently.

Of at least equal significance, only some of the dollars paid by the senior lender will be the functional equivalent of cash, because the senior lender is not really paying any money at all. The successful lender pays the successful bid price by crediting the debt owed to the lender, not by coming out of pocket with actual cash. The dollars of debt first bid by the construction lender—up to the lender’s perception of the fair market value of the project—probably equate reasonably well to the value of a like number of dollars of actual cash dollars bid by a true third-party bidder. Once the bidding moves above the fair market value of the project, however, the value equivalence breaks down. Until then, if the lender were to let a competing cash bidder win the auction, the lender would be leaving value behind. After the bidding reaches the lender’s estimation of the current fair market value of the collateral, the cost of bidding additional dollars—the cost of bidding “deficiency dollars”—is measured by the value to the lender of preserving the right to seek payment of the deficiency from alternate sources of recovery. If the probability of collecting any deficiency is low, the true cost to the construction lender of credit-bidding “too much” is not the same as the cost a cash bidder suffers if it were to pay too much. A lender bidding deficiency dollars may be bidding with funny money, depending on how it evaluates the prospect of collecting the deficiency from secondary sources of collection.

The lender’s decision to bid too much, in this context, will depend upon the lender’s assessment of the relative value of speedy acquisition of title to the project, in comparison to the opportunity cost of giving up the lender’s alternate sources of recovery for the deficiency. The lender will evaluate the prospect of receiving a dividend from the estate on account of its deficiency claim, as well as the prospect of obtaining and collecting a judgment from third parties, such as nondebtor co-obligors, guarantors, alter egos of the borrower, and, perhaps, others. After assessing the existence and probabilities of collection from secondary sources, it is normal for a lender to see the advantage of reducing, if not giving up, its prospects of recovery from secondary sources, if there are any, in exchange for ready access to its collateral.

In this economic environment, it may be that the deficiency dollars bid by the lender are essentially cost-free to the lender. Even if there are creditworthy guarantors or defendants, the costs, delays, and uncertainties of collection force the lender to discount the face value of the deficiency claims. Depending on the facts of the particular case, the cost of bidding deficiency dollars may be somewhere between zero and the par amount of the deficiency, but unless at least one secondary source of recovery is the functional equivalent of pledged cash in the possession of the lender and not burdened by any stay, chances are a heavy discount of those deficiency dollars will be appropriate.

In *Clear Channel*, the construction lender was the first and only bidder. There is no mention in the reported decision whether evidence of the value of the project was offered at the sale hearing. That omission, plus the obvious conclusion that an existing senior secured lender is, by definition, not free from compulsion, makes the BAP’s analysis of Section 363(f)(3) of limited persuasive value in future cases in which appropriate evidence is submitted regarding project value and deficiency amounts. It may well be that the trustee and construction lender in *Clear Channel* believed that the fair market value of the project was greater than the claim of the construction lender or were motivated by tax or other strategies to establish a high basis in the asset. Whatever unique goals may have motivated their litigation strategy, there is no reason that future litigants or future courts should conclude that *Clear Channel* stands for the proposition that a credit bid price is a cash equivalent indicator of fair value, as a matter of law. *Clear Channel* should be limited to the facts of that case, as presented in that case, and not for a dubious valuation proposition that was neither disputed by the parties nor resolved by the BAP.

The BAP also rejected the argument that the sale qualified under Section 363(f)(5); the *Clear Channel* bankruptcy court apparently found that, if the objecting party’s interest is a lien, the bankruptcy court need not identify a proceeding in which the objecting creditor could be compelled to accept a money payment in satisfaction of its interest, because a lien can always be satisfied by paying the value of the lien. The BAP reversed on this point, holding that Subsection (f)(5) requires proof of the existence of a proceeding in a nonbankruptcy forum in which the objecting creditor could be compelled to accept less than payment in full as a full satisfaction of the lien (or other interest) and that the interpretive error led to the bankruptcy court’s failure to make a finding regarding the existence of such a proceeding. Thus, the case was remanded to the bankruptcy court so that the parties could present their respective posi-
tions and obtain a ruling from the bankruptcy court on the question whether such a proceeding existed.

After remark, the parties elected not to pursue the issue further, so there are no subsequent rulings of either the bankruptcy court or the BAP to shed light on the question whether such a proceeding exists. This means the Clear Channel decision leaves the door wide open for subsequent litigants in new cases to attempt to identify nonbankruptcy proceedings in which a junior lien holder could be compelled to accept a money satisfaction of its interest in the collateral.

Judicial Foreclosure

Judicial foreclosure would seem to be the procedure. Judicial foreclosure is a proceeding in equity brought in a nonbankruptcy forum (typically, a California Superior Court for property located in California) by a holder of a mortgage or deed of trust against the owner of the property and all parties claiming an interest in the property under the owner (or its predecessor in interest), such as holders of junior consensual and mechanic’s liens. If the plaintiff properly pleads its complaint and prevails at trial or summary judgment, the Superior Court will issue a judgment of foreclosure and order for sale that will direct the sale under a writ of sale at public auction. The court, alternatively, may order the receiver to sell the property. The plaintiff is entitled to credit-bid up to the full amount of its claim against the mortgagor, as determined in the judgment of foreclosure and order for sale.

The judgment of foreclosure and order for sale will determine the relative priority of all lien claimants joined in the action. It will also direct the application of the net proceeds of sale first to the plaintiff (assuming it has the highest priority), with any excess to be paid first to the junior lien holders in order of their judicially determined priority and then, if any excess remains, to the mortgagor. The sale extinguishes the plaintiff’s lien and the liens of all junior lien holders who have properly been joined in the action. Even junior lien holders omitted from the lawsuit may have their liens extinguished in a subsequent foreclosure action brought by the successful bidder.

If the judgment of foreclosure and order for sale determines that no deficiency is available, the successful bidder will obtain a deed of sale at the conclusion of the sale and payment of the bid price. If redemption is permitted, the successful bidder will receive a certificate of sale upon payment, which will be replaced by a deed of sale upon expiration of the applicable redemption period, if the property is not redeemed before that time. Junior lien holders do not have a post-sale statutory right of redemption. Their liens do not reattach even if the mortgagor exercises its statutory right of redemption.

Would judicial foreclosure qualify under the BAP’s reading of Section 363(f)(5)? The statutory construction methodology employed by the BAP is elaborate, but can be summarized as limiting qualifying nonbankruptcy proceedings to be those covered by an interpretation that 1) is of a breadth that complements the alternative tests specified in Section 363(1)-(4), 2) does not overlap with those tests, and 3) is consistent with congressional intent. Judicial foreclosure would appear to satisfy at least two, if not all three, of these requirements. Certainly, judicial foreclosure appears to be encompassed by a literal interpretation of the plain text of the statute. Judicial foreclosure undeniably is a proceeding by which the objecting junior lien holder could be forced to accept a monetary payment (which may be nil, depending on the net sales proceeds generated) in satisfaction and extinguishment of its lien. Judicial foreclosure clearly complements the other four subsections. It is an alternative, nonbankruptcy method for selling free and clear of liens in situations in which an auction would not generate a price sufficient to pay an amount greater than the aggregate value of all liens, and thus complements Section 363(f)(3).

As for the absence of overlap, it bears noting that, unlike all the general tests for a sale free and clear of liens, a lender’s right to obtain a decree of foreclosure and order for sale does not depend in any fashion on proof that the property will be sold for fair market value. No doubt, the lender is given a strong incentive to bid up to its perception of fair market value, because the amount of its deficiency judgment will be determined in a post-sale fair value hearing—not the bid price—but the debtor will be able to redeem the property from the sale during the following year by paying only the bid price, not the judicially determined fair market value. That being said, it is the lender’s absolute right to bid what it chooses at the sale, regardless of the fair value of the project. In this sense, there is uniqueness, not overlap, in an interpretation of Section 363(f)(5) that relies on the judicial foreclosure analog.

When Clear Channel was first handed down, it created consternation among counsel to creditors and debtors, as it seemed to eliminate an emerging means to resolve problem real estate loans in an efficient, rational, and organized manner. On reflection, however, it seems that a preconfirmation sale free and clear of liens remains a viable option, in an appropriately organized manner. On reflection, how-
stalking horse bidder is a credit-bidding senior secured lender. Moreover, the BAP not only failed to address the judicial foreclosure analog but also remanded the case to the bankruptcy court so that the parties could attempt to identify and argue potentially qualifying nonbankruptcy proceedings. The door is, thus, left open for parties to argue the judicial foreclosure analog in other cases. Rumors of the death of the 363 sale are greatly exaggerated.

1 A junior lien of any variety can gain at least partial priority over a previously recorded deed of trust if, prior to foreclosure, the senior lender has made so-called optional advances (see Turner v. Lytton Sav. & Loan Ass’n, 242 Cal. App. 2d 457 (1966)) or has made certain modifications to the senior loan without the consent of junior lien claimants (see Lennar Northeast Partners v. Buice, 49 Cal. App. 4th 1576 (Cal. App. 3d Dist. 1996)). Additionally, mechanic’s liens may have statutory priority—even if the claim of lien is recorded after recordation of the deed of trust (CIV. CODE §3134) or if site improvement loans and liens are involved (CIV. CODE §3137). Even improperly asserted claims of priority can give junior lien claimants the power to impose significant delay and, thus, give them leverage to extort payments from those holding interests that actually have value.

2 As a general proposition, a debtor in possession in a chapter 11 bankruptcy case has the powers of a trustee. 11 U.S.C. §1107. For the sake of simplicity, the term “trustee” in this article applies also to a debtor in possession if no trustee has been appointed in a chapter 11 case.


4 Clear Channel Outdoor, Inc. v. Knupfer (In re PW, LLC), 391 B.R. 25 (9th Cir. BAP 2008).

5 Usually the auctions are live, open auctions in which the bankruptcy judge acts as the auctioneer for an all-cash sale. Occasionally, sealed bid auctions and partially deferred or noncash consideration may be approved if that is more likely to generate the best recovery.

6 The sale is advertised or otherwise marketed so that others interested in the property will have an opportunity to bid—and possibly bid higher than the opening bid of the stalking horse. The stalking horse will often insist upon 1) a break-up fee to be paid to the stalking horse if it is outbid at the auction, to compensate for the fees, expenses, and time it expended on preparing for the transaction, and 2) a minimum over-bid amount in addition to the break-up fee, set high enough to give the stalking horse an advantage but not so high as to discourage competitive bidding.

7 11 U.S.C. §363(k) permits a lender to credit bid at a sale.

8 This is not to say that participants can conceal material arrangements or agreements affecting the sale from the Bankruptcy Court. Such concealment would likely be a felony under 28 U.S.C. §152(6). Bidding arrangements that may invalidate a sale outside of bankruptcy can be agreed to without jeopardy if fully disclosed to and approved in advance by the Bankruptcy Court in the context of a Section 363 sale.

through a provision in a plan. (10)

litigation in an adversary proceeding and not

Procedure provide that a “proceeding to determine

the validity, priority or extent of a lien” is an adver-

sary proceeding.

(11)


(12)


(13)


(14)

14 Rule 7001(2) of the Federal Rules of Bankruptcy

Procedure.

(15)

15 1129(b) of the code, because that would either gut or

render superfluous the protections afforded by the dis-

bursement process.

(16)

16 The BAP ruled that the qualifying legal or equitable pro-

cessing cannot include a cramdown under Section

363(f)(3).

(17)


(18)

18 See SLW Capital, LLC v. Mansaray-Ruffin (In re

Mansaray-Ruffin), 530 F. 3d 230, 237 (3d Cir. Pa. 2008) (Lien invalidation may be accomplished only

through litigation in an adversary proceeding and not

through a provision in a plan.).

(19)

19 Clear Channel Outdoor, Inc. v. Knupfer (In re PW,

LLC), 391 B.R. 25, 45-47 (9th Cir. BAP 2008).

(20)

20 The BAP decision in Clear Channel has become

final. Even those bankruptcy courts in the Ninth Circuit

that do not deem themselves bound by the BAP

nonetheless characterize BAP decisions as highly per-

suasive. See Bank of Maui NA v. Estate Analysis, Inc.,

904 F. 2d 470 (9th Cir. 1989) (stating, in dictum, that

BAP decisions are not binding on district courts,

acknowledging that the Ninth Circuit had not decided

whether BAP decisions were binding on bankruptcy

courts, and declining to decide the issue). See also

Zimmer v. PNB Lending Corp., 315 F. 3d 1220 (9th Cir.

2002) (acknowledging, without resolving, the unsettled

law in this area). Not surprisingly, the BAP has held that

its decisions are binding on the bankruptcy courts. In

re Windmill Farms, Inc., 70 Bankr. 618 (9th Cir.

1987). Approximately two-thirds of the published and

unpublished decisions of bankruptcy courts in this cir-

cuit that cite the Bank of Maui decision state they are

not bound by the BAP; the remainder state the contrary.

Those that deem themselves not bound nonetheless

characterize BAP decisions as highly persuasive. See, e.g., In re Atemam, 259 B.R. 371 (Bankr. C.D. Ca.

2001); In re Enriquez, 244 B.R. 156 (Bankr. S.D. Ca.

2000).

(21)


(22)

22 See APPRAISAL INSTITUTE, THE DICTIONARY OF REAL


(23)

23 Tax and accounting issues may also play a role in the

lender’s bidding strategy, making comparison to the

prices paid by cash bidders all the more problematic.

(24)

24 Traditional appraisal methodology requires an

appraiser to adjust a financed purchase price to its all

cash equivalent when the financed transaction is used

as a comparable sale in the valuation. See APPRAISAL

INSTITUTE, THE APPRAISAL OF REAL ESTATE 373-380


(25)

25 The price paid by a successful bidder may exceed fair value if it is paying for a control premium

or other nonmarket value.

(26)

26 BAP decision state they are

not bound by the BAP; the remainder state the contrary.

Those that deem themselves not bound nonetheless

characterize BAP decisions as highly persuasive. See, e.g., In re Atemam, 259 B.R. 371 (Bankr. C.D. Ca.

2001); In re Enriquez, 244 B.R. 156 (Bankr. S.D. Ca.

2000).

(27)

27 5 B. WITKIN, CALIFORNIA PROCEDURE, PLEADING,

INSTITUTE, THE APPRAISAL OF REAL ESTATE 373-380


(28)

28 Traditional appraisal methodology requires an

appraiser to adjust a financed purchase price to its all

cash equivalent when the financed transaction is used

as a comparable sale in the valuation. See APPRAISAL

INSTITUTE, THE APPRAISAL OF REAL ESTATE 373-380


(29)

29 Id. at §3.32; C ODE CIV. PROC. §§729.010, 729.070,

706.020, 701.630.

(30)

30 Id. at §3.74. See also 55 CAL. JUR. 3D, RECEIVERS §75

(2004); CIV. CODE §568.

(31)

31 Id. at §3.77.

(32)

32 Id. at §3.85.

(33)

33 Id. at §3.87.

(34)


(35)

35 1129(b) of the code, because that would either gut or

render superfluous the protections afforded by the dis-

bursement process.

(36)

36 Id. at §3.79.

(37)

37 Id. at §3.90.

(38)

38 Clear Channel Outdoor, Inc. v. Knupfer (In re PW,

LLC), 391 B.R. 25, 37-39 (9th Cir. BAP 2008).

(39)

39 This is not to say that a bankruptcy court will allow the
developer to abandon its fiduciary duty to exercise rea-

sonable business judgment in negotiating a minimum

opening bid. It is merely to address the BAP’s require-

ment for an absence of overlap. Even if there were over-

lap, it is important to remember that “[s]urplusage

does not always produce ambiguity and our preference

for avoiding surplusage constructions is not absolute.”

Lamie v. United States Treasury, 540 U.S. 526, 535

(U.S. 2004).
A significant percentage of divorcing parents continue their conflicts over custody well after obtaining a judgment on custody and visitation. While this percentage declines over time, many so-called high-conflict parents remain mired in adversarial litigation for years after divorce. These parents utilize much of the court’s resources and entangle their children in a process that makes them more likely to develop emotional and behavioral problems.

In addition to the grave emotional costs, the financial burden on the family can be ruinous, since these ongoing disputes incur extraordinary legal fees as well as the costs of custody evaluations, psychological testing, therapy, supervised visitation, and drug and alcohol monitoring. These conflicts also can result in loss in employment productivity due to emotional stress and the time required to attend and prepare for court hearings.

Custody and visitation can be modified after the judgment as the needs of the children and parents change. Ironically, this ability to modify custody or visitation orders can become a vehicle for additional battles for those parents inclined to prolong the litigation war. As children develop, the parenting plan approved by the court may need to change accordingly. Thus some flexibility is ideal. Indeed, case law allows for the modification of parenting plans. Still, given children’s need for stability and the negative impact of parental conflict, parents should not only have a clearly defined parenting plan but also should avoid unnecessary tinkering with their time-sharing arrangements and the myriad other details related to parenting. When changes are necessary, parents may consult with mental health professionals, mediators, and attorneys to work out the details and avoid litigation.

However, if a return to court is necessary, parents can still try to avoid a new, protracted struggle for custody. One avenue to explore involves refocusing a request for a change in custody to a change in visitation. Another method is to engage the assistance of a parenting plan coordinator (formerly a special master).

An initial custody determination, which is based upon the child’s best interest, mandates the physical and legal custody of a child and allocates custodial time between the parents. Parents may still be able to change this arrangement through modification proceedings.

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ceedings. The general and oft-cited rule is that once the trial court has entered a final or permanent custody determination, modification of custody is appropriate only if the parent seeking modification demonstrates a “significant change in circumstances” so that a different custody arrangement would be in the child’s best interest. However, this change of circumstances rule does not apply when a parent is seeking to change the time-share arrangement only, not physical custody, and does not apply when parents share joint custody.

Careful reading of the developments in case law regarding modification of child custody arrangements reveals opportunities for avoiding the stringent change of circumstances test. In In re Marriage of Carney, the California Supreme Court placed extreme importance on existing custodial arrangements and held that parents seeking to change established parenting plans must establish a “persuasive” and “substantial” change of circumstances to warrant a modification of the existing parenting plan. Under Burchard v. Garay, the California Supreme Court narrowed the application of the change-of-circumstances standard of proof, holding that it only applied if there is a prior judicial determination of custody. Under Burchard, a stipulated parenting plan—one that is not court imposed—did not qualify as a prior judicial determination, and thus the change-of-circumstances standard of proof did not apply. A decade later, in Montenegro v. Diaz, the supreme court revisited the impact of stipulated custody plans and held that a stipulated custody order will be deemed a final adjudication if it expressly states the parties’ intention for it to be the final determination of custody. However, if the stipulation does not contain a “clear, affirmative indication” of the parties’ intent that it is their final custody agreement, the change-of-circumstances standard of proof does not apply, and the party seeking a change of custody need only show that the change is in the best interests of the child.

The Birnbaum Standard

Separate from Carney and its progeny addressing a change of custody is a line of cases in which the courts changed only the custodial time allocation, not custody itself. This shift in focus brought a significant alteration in the applicable standard of proof. When a parent seeks a change in the parenting schedule but does not seek to change the physical custody arrangement (sole to joint and joint to sole), only the best interests standard applies. Specifically, the parent need not establish a change of circumstances.

The first in this line of cases was In re Marriage of Birnbaum, in which a stipulated judgment awarded the parents joint legal and physical custody of their three minor children, with the children living with the mother on weekdays and with the father on weekends and Wednesday afternoons during the school year. In modification proceedings based on the mother’s relocation to a different part of the county, the mother sought sole custody of the children and to limit the father’s visitation time to alternate weekends. The father responded the county, the mother sought sole custody of the children and to limit proceedings based on the mother’s relocation to a different part of the child that there be a change.” The rationale for this rule was the fact of “a kind to render it essential or expedient for the welfare of the child.” The rationale for this rule was the best interest standard applies. Specifically, the parent need not establish a change of circumstances rule does not apply to a modification request seeking only a change in the parenting or visitation arrangement. This change of circumstances rule does not apply when a parent is seeking to change the time-share arrangement only, not physical custody, and does not apply when parents share joint custody.

In 2008, in In re Marriage of Lucio, the appellate court followed the line of reasoning in Birnbaum and Enrique M., regarding the distinction between a change of custody and a change of parenting schedule. The Lucio court held that the change of circumstances rule does not apply to a modification request seeking only a change in the parenting or visitation schedule.

The dissolution judgment awarded the mother sole physical custody of the children and granted the father monitored visits on Sundays. The father requested a change in the parenting and visitation schedule to permit him unmonitored visits from Friday night to Sunday night on alternate weeks. The trial court effectively denied the father’s request because the father had not shown a change of circumstances. The appellate court reversed, concluding that the best interests test governed because the father’s requested changes to the visitation schedule would not result in either an actual or a de facto change in custody. Furthermore, the requested alteration in the visitation schedule would not have disrupted the established patterns of care and emotional bonds between the children and their mother and would not have destabilized the arrangement for sole physical custody.

Thus, the change of circumstances rule does not apply when a parent requests only a change in the parenting or visitation arrangement that is neither a change in custody nor disrupts the established patterns of care. In such cases, the best interests test applies.

Arguably, most parents have joint physical or joint legal custody orders. Though changes in the parenting plan may occur frequently, as noted in Burgess and Enrique M., modifications of time allocation can obviate time-consuming and costly custody litigation, which may itself “be detrimental to the welfare of minor children because of the uncertainty, stress, and even ill will such litigation tends to generate.” Thus, parents should carefully consider the focus and intent of their modification requests.

Parenting Plan Coordinators

In addition to more carefully tailoring requested modifications, parents also can reduce conflict by considering a number of alternatives to litigation. These include mediation, which is free through court conciliation services or at a cost with private mediators; collaborative family law; coparent counseling and education courses; and parenting plan coordinators. The Association of Family and Conciliation Courts (AFCC) Task Force on Parenting Coordination explains that “parenting coordination is a child-focused alternative dispute resolution process in which a mental health or legal professional with mediation training and experience assists high-conflict parents to implement their parenting plan by facilitating the resolution of their disputes in a timely manner, [by]
educating parents about children’s needs, and, with prior approval of the parties and/or the court, [by] making decisions within the scope of the court order or appointment contract.”47 A parenting plan coordinator is not the parties’ therapist but acts in “an ADR [alternative dispute resolution] activity, a legal-psychological hybrid role.”48 The coordinator establishes “a strong, positive therapeutic and psycho-educational alliance” that focuses on the children’s best interests and a reorganized family.49 Instead of litigating parenting issues and having the courts act as “super-parents,”50 the parenting plan coordinator—a neutral who specializes in custody and visitation issues—takes the time to get to know the family and makes decisions quickly to resolve conflicts.51 A wide range of issues can lead to disputes in need of resolution, including psychotherapy, religion, summer camp choice, and even a child’s clothes or appearance.

The AFCC provides the Model Standards and Guidelines for the parenting plan coordinator’s role, practice, and training as well as the Model Standards for Divorce Mediation.52 California has no statutory authority for appointing parenting plan coordinators or for their training. Absent an agreement by the parties, the court cannot appoint a coordinator. When the parties agree, California mandates that the appointment be by a written stipulation and order.53 Contractual arbitration law may be the most applicable legal authority for appointment of a coordinator.54 A sample Stipulation and Order Appointing Parenting Plan Coordinator has been developed by the Family Law Section of the Los Angeles County Bar Association.55 The types of decisions set forth in the stipulation include:

1) The clarification of ambiguous or uncertain provisions in the court-ordered parenting plan.
2) Establishing times, places, and conditions for exchanges of a child under a court-ordered parenting plan.
3) Occasional changes to the visitation or parenting time schedule for holidays, vacations, or special days.
4) Permanent changes, minor or significant, to the parenting schedule.
5) Determining the child’s participation in school or extracurricular activities or programs.
6) Information exchanges between households.
7) Travel orders.
8) Childcare decisions.
9) Medical decisions, including services for special needs children.
10) Choice of schools.56

Parents must agree on the scope and authority of the appointment of a parenting plan coordinator. The agreement is set forth in the stipulation. The coordinator makes parenting decisions after consulting with the parents (and others, if needed) and gives the parents notice of his or her decisions. The coordinator typically sends a written decision briefly explaining his or her recommendations and findings.

This decision will then be formally submitted on a Judicial Council form—a Notice of Decision—and submitted to the court for adoption as an order of the court. A party may contest the Notice of Decision within 30 days after the court’s entry of the Notice of Decision.57 A party begins this process by filing an order to show cause.58 In addition to setting forth the issues that will be within the scope of the coordinator’s decision-making authority, the stipulation designates each issue as a Level 1, 2, or 3 decision.59 Level 1 decisions involve short-term practical matters and are typically time-sensitive, such as holiday schedule changes or the interpretation or clarification of the parenting plan. Level 1 decisions are reviewed by the court only if a parent files for a hearing within 30 days after entry of the Notice of Decision.60 If a parent does not timely file for review, the right to challenge the coordinator’s decision is waived.61 If contested, the court may reverse or modify a Level 1 decision if the challenging parent shows that the decision exceeds the authority of the coordinator, exceeds the jurisdiction of the court, or is erroneous as a matter of law, or proves by a preponderance of the evidence that the decision is not in the best interests of the child.62

Level 2 decisions typically have a long-term effect but do not make major changes to the roles of parents as decision makers or significantly change the percentage of time that the child is in each parent’s home.63 Parents may designate Level 2 decisions as Level 1 decisions.64 The same review process for Level 1 decisions applies to Level 2 decisions.65

Level 3 decisions involve major changes to the parenting plan. Only certain types of decisions are customarily designated as Level 3 decisions. These are decisions based upon a stipulation of the parents, or a court order made at a trial, or after a hearing on an order to show cause, or a motion. If the parties do not stipulate to a resolution, the parenting plan coordinator may make recommendations concerning Level 3 issues, but the coordinator cannot make any decisions or file and serve a Notice of Decision for Level 3 issues.66 The coordinator may make written recommendations to the court about a Level 3 decision after giving the parents a reasonable opportunity to state their views.67 As set forth in the Association’s stipulation, a court must admit the findings and recommendations of the coordinator into evidence as an expert opinion, subject to cross-examination. Hearsay objections are waived in the stipulation.68

In determining what level of decisions to submit to the parenting plan coordinator in the stipulation, the parents should weigh the value of reduced conflict against the cost of continued litigation. To reduce conflict, parents may choose to carefully confine the scope of the coordinator’s authority to specific issues, make all of those issues Level 1
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decisions, and not contest the decisions even if they disagree. If the coordinator assists the high-conflict parents with disengaging from their ongoing battle, the parents have a “greater likelihood of succeeding and having a positive impact on the children’s adjustment in these [reformulated] families.” The goal of the parenting plan coordinator is to move parents away from adversarial litigation into a relationship or process that establishes new rules for coparenting, enables parallel parenting, creates more stability for the parenting plan, allows greater exchange of information between the parents, and moves quickly toward decisions in the child’s best interests.

Given the decision-making power of the parenting plan coordinator, careful consideration must be given to the choice of the coordinator. A coordinator should have experience in drafting clear orders, resolving problems, and understanding the needs of children.

The effects of sustained conflict on children and on parents are demonstrably negative. A decision by a parenting plan coordinator may be the best outcome for everyone, even if the decision contains some disappointing elements for both parents. Parents in conflict can act in the best interests of their children and themselves by avoiding custody litigation and stipulating to a parenting plan coordinator. Alternatively, parents can narrowly focus their requests for additional time with their children as a modification for visitation and not seek a modification for custody.

5 Id.
6 Fam. Code §3022.
8 Fam. Code §§3011, 3020, 3022, 3040.
9 Fam. Code §§3022, 3027. See also Berke, supra note 6.

For more information, see Los Angeles Collaborative Law Association: http://www.lacfla.org. See also International Academy of Collaborative Professionals, http://www.collaborativepractice.com. A collaborative practice or collaborative divorce (also called no-court divorce) offers divorcing couples the support, protection, and guidance of lawyers working with child and financial specialists, divorce coaches, and other professionals with the expectation that the case will not go to court.


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The parenting plan coordinator is useful for 1) "parents with severe personality disorders who become locked in immutable impasses and are chronically litigating"; 2) parents "where there is less character pathology but great difficulty making important mutual and timely decisions" (regarding, for example, infants and young children who require reworking of the parenting plan due to their "rapidly changing developmental needs" or special needs); and 3) abusive parents or intermittently mentally ill parents who require monitoring. JOHNSTON & ROSEBY, supra note 1, at 246.


See CAL. CONST. art VI, §1; In re Marriage of Olson, 14 Cal. App. 4th 1, 3 (1993); Russ v. Thieriot, 53 Cal. App. 4th 1197 (1997) (court cannot be divested of its judicial power); FAM. CODE §3160; EVID. CODE §730; CODE CIV. PROC. §§1280 et seq. (authority for parties’ agreement); See also Christine A. Coates, Parenting Coordination for High-Conflict Families, 41 FAM. CT. REV. 1, 3, 6 (2004).

Leslie Ellen Shear, In Search of Statutory Authority for Parenting Coordinator Orders in California: Using a Grass-roots, Hybrid Model Without an Enabling Statute, 5 J. CHILD CUSTODY 88, 94-95 (2008); see CODE CIV. PROC. §§1280 and seq., authority for parties’ agreement. See also Christine A. Coates, Parenting Coordination for High-Conflict Families, 41 FAM. CT. REV. 1, 3, 6 (2004).

Shear notes that contractual arbitration has the advantage of offering statutory civil immunity under Code of Civil Procedure §1280.1 and common law civil immunity. Although Evidence Code §703.5 bars testimony by the arbitrator, the Los Angeles County Bar Association’s parenting plan coordinator stipulation (see text and notes, infra) expressly allows the admissibility into evidence of the written findings and recommendations of the coordinator as expert opinion testimony subject to the right of cross-examination. In the stipulation, the parents waive both the right to object to the coordinator’s report as being hearsay and the right to object to the hearsay statements contained therein, but they retain the right to attack the weight, sufficiency, and reliability of the evidence. The stipulation preserves the jurisdiction of the family court to review and reverse decisions of the coordinator, which may help insulate the orders adopting the coordinator’s decisions against reversal. Shear at 96.

Shear notes that contractual arbitration has the advantage of offering statutory civil immunity under Code of Civil Procedure §1280.1 and common law civil immunity. Although Evidence Code §703.5 bars testimony by the arbitrator, the Los Angeles County Bar Association’s parenting plan coordinator stipulation (see text and notes, infra) expressly allows the admissibility into evidence of the written findings and recommendations of the coordinator as expert opinion testimony subject to the right of cross-examination. In the stipulation, the parents waive both the right to object to the coordinator’s report as being hearsay and the right to object to the hearsay statements contained therein, but they retain the right to attack the weight, sufficiency, and reliability of the evidence. The stipulation preserves the jurisdiction of the family court to review and reverse decisions of the coordinator, which may help insulate the orders adopting the coordinator’s decisions against reversal. Shear at 96.

Other issues for inclusion in the stipulation for a parent...
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**C A B I N E T N O T E S**

16 See Parenting Plan Coordination Stipulation, Special Needs Coordinator, available at http://www.specialneedscoordinator.com/docs/PPC%20Stipulation2007.pdf; see also the Los Angeles County Bar Association’s sample stipulation, supra note 54. Since parents are stipulating to the appointment of the parenting plan coordinator, the coordinator does not violate the mandate that judicial officers cannot delegate decision-making authority on child custody issues. The Association’s stipulation includes language that the court retains jurisdiction to review decisions of the coordinator and all other issues related to the parenting plan.

17 The Los Angeles County Bar Association’s sample stipulation, supra note 54. It is important that a parenting plan coordinator submit the Notice of Decision and provide the parents with a conform cauliflower. In practice, some coordinators do not follow these rules, so parents should carefully choose a coordinator who knows the rules and follows the Association of Family and Conciliation Court guidelines.

18 The Los Angeles County Bar Association’s sample stipulation, supra note 54.

19 Id.

20 Id. The stipulation refers to the time in which a parent may contest the Notice of Decision as commencing from the date of “entry of the order.” Parties may seek to clarify this as the date when the order is filed by the court. They may even wish to change the time period so that it begins when they are given notice by facsimile, mail, or whatever method the parties specifically and clearly identify.

21 The Los Angeles County Bar Association’s sample stipulation, supra note 54.

22 Id.

23 Id.

24 Id. Level 1 decisions involve rapid communication between the coordinator and the parents. In Level 2 decisions, the coordinator must provide the parents with opportunities to state their views and provide information before the coordinator makes a decision.

25 The Los Angeles County Bar Association’s sample stipulation, supra note 54.

26 Id. Level 3 decisions include: relocation of the child, travel to countries that are not signatories to the Hague Convention on the Civil Aspects of International Child Abduction, major medical decisions, school selection, counseling, participation in custody evaluations for modification of the custody plan, or permanent modification of legal custody.

27 Id.

28 Id.

29 Sullivan, supra note 1, at 4, 11.

30 “Parallel parenting” is a term for parenting in which the parents have little or no interaction with each other. In this circumstance, the parenting plan should be written in detail, with no loopholes subject to interpretation. The parents do not engage in flexible scheduling and work independently for their child’s best interests. Both households function independently. Id. See also Statt, supra note 54.

31 E-mail communication can be monitored by the Parenting Plan Coordinator, either by copying the Coordinator on the e-mail or by e-mailing the Coordinator for editing before the e-mail is sent to the other parent, or by using the Coordinator as an intermediary for forwarding the e-mail to the other parent. Id. Sullivan, supra note 1, at 4-24, 18.

32 Id. at 12.
2008 was a year of great highs and lows in legal ethics. Venerable California law firms were not immune from the collapse of the economy, as 118-year-old Heller Ehrman and 84-year-old Thelen voted to dissolve and other firms announced mergers, defections, layoffs, delayed employment starts, cancellations of bonuses, and salary freezes. Moreover, prominent lawyers were punished for serious misconduct.

Convicted of conspiring to wiretap his client Kirk Kerkorian’s former wife, Terry Christensen was sentenced to three years in prison and fined $250,000 by U.S. District Judge Dale Fischer, who excoriated Christensen for “deliberately, repeatedly and happily violating the law” and failing to show remorse. U.S. District Judge John Walter sentenced Melvyn Weiss, cofounder of the class action law firm Milberg Weiss, to 30 months in prison and ordered him to forfeit $9.75 million and pay a $250,000 fine for secretly paying class representatives. Judge Wallace Tashima, sitting as a special master, found that Thomas Girardi, Walter Lack, and their associates had filed suit to enforce a $489.4 million Nicaraguan court judgment against two nonparties based on false and incomplete translations of the foreign court records, ghost-written expert declarations, and misleading briefs, and recommended sanctions. After Judge Tashima made his findings, the Ninth Circuit Court of Appeals opened a disciplinary matter and appointed Hastings College of Law Professor Rory Little as an independent prosecutor.

Beleaguered U.S. District Judge Manuel Real was removed from five cases in 2008 by the Ninth Circuit, the Federal Circuit, and the U.S. Supreme Court. Beleaguered U.S. District Judge Manuel Real was removed from five cases in 2008 by the Ninth Circuit, the Federal Circuit, and the U.S. Supreme Court. However, the Ninth Circuit restored Real to active duty.

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by John W. Amberg and Jon L. Rewinski
Conflicts of Interest

With continuing lawyer mobility and law firm consolidation, it is no surprise that conflicts of interest continue to be a hot topic. The fundamental principles set forth in Rule 3-310 of the Rules of Professional Conduct have not changed. During 2008, the Second and Fourth District Courts of Appeal had occasion to analyze them in published opinions.

In Sharp v. Next Entertainment, Inc.,12 the defendants—producers of reality television programs—moved to disqualify the lawyers representing the named plaintiffs in a putative class action alleging that the defendants failed to pay class members for overtime in accordance with applicable law. The law firm representing the plaintiffs also represented the Writers Guild of America in unrelated matters. The guild wanted to unionize reality TV employees and set up the meetings between its lawyers and the employees that led to the lawsuit. The guild also agreed to pay the legal fees and costs incurred in the class action.

Arguing that the plaintiffs and the guild had conflicting interests, the producers moved to disqualify the plaintiffs’ law firm. The court denied the motion but ordered the law firm to erect an ethical screen that would preclude communications about the class action between the lawyers handling the class action and the lawyers handling the guild’s matters, with an exception for the issue of fees and costs, because the guild had agreed to pay them. The Second District Court of Appeal affirmed.

The trial court found that the Writers Guild and the plaintiffs did not have conflicting interests within the meaning of Rule 3-310 of the Rules of Professional Conduct. The court of appeal declined to review this finding because it concluded that the guild and the plaintiffs had signed consents waiving any actual or potential conflicts and, therefore, it was unnecessary to decide whether there was a conflict. The Rules of Professional Conduct do not specifically address conflict waivers in the context of a class action,13 and neither the California Supreme Court nor a California court of appeal had done so in a published case before Sharp.

In Sharp, the Second District held that the law firm was not required to obtain conflict waivers from all putative class members. It only needed to obtain waivers from the named plaintiffs and the guild.14 The court of appeal reasoned that because the case had not yet been certified, unnamed members of the putative class were not parties. Obtaining consent from all putative class members would have been impractical, and requiring all putative members to sign conflict waivers would have, in effect, created an inappropriate opt-in class action. Further, if there are conflict-of-interest issues, the ability of a named plaintiff to represent class members adequately would be sufficiently vetted through the class certification process.15

In Gong v. RFG Oil, Inc.,16 the Fourth District Court of Appeal considered a motion to disqualify defense counsel because of a conflict arising in litigation over the management of a closely held corporation. Two brothers owned all the defendant corporation’s stock—one held 51 percent, the other, 49 percent. The majority owner managed the business. After a dispute arose between the brothers, the minority owner sued the company and his brother, alleging that his brother had mismanaged the business, wasted corporate assets, used company assets to buy real estate for himself, and improperly ran him out of the business. He asserted claims for declaratory relief, breach of fiduciary duty, wrongful termination, and dissolution.

With a conflict waiver in hand, a lawyer attempted to represent both defendants—the majority-owning brother and the company. Indeed, as a practical matter, to communicate with the company, the lawyer had to communicate with the majority-owning brother. Arguing that the interests of his brother and the company were in conflict and that the conflict could not be waived, the minority-owning brother moved to disqualify the defendants’ lawyer. Although the trial court denied the motion, the Fourth District Court of Appeal issued a writ, ordering the trial court to grant the motion.

In cases involving concurrent representation of clients with actual or potential conflicting interests, the primary concern is the duty of loyalty to the lawyer who owes to each client.17 The appellate court reasoned that even though the plaintiff had not asserted a derivative claim, his allegations of waste and mismanagement created an actual conflict that prevented a single lawyer from satisfying a duty of loyalty to both the company and the majority owner. For example, if the plaintiff established that his brother had used corporate assets to buy real estate for himself, his brother would owe money to the company. An actual conflict between the interests of the two defendants precluded one lawyer from jointly representing them.

In another matter, Justice Arthur Gilbert, writing for the Second District Court of Appeal, continued his tradition of deciding attorney misconduct cases without reference to the Rules of Professional Conduct or the State Bar Act. The appellate court affirmed judgment against an attorney, Eddie B. Jamison, for malpractice, breach of fiduciary duty, and financial abuse of an elder in Wood v. Jamison.18 The attorney simultaneously represented a 78-year-old woman and an impostor claiming to be the woman’s nephew. During the representation he helped procure a $250,000 loan at 18.41 percent interest for his elderly client, secured by her house, so she could invest in the phony nephew’s night club. The lawyer received $14,000 from the loan proceeds, which he did not disclose. The woman defaulted on the first installment. After she died, the lender moved to foreclose on her home, and the executor of her estate sued the lawyer.

The appalled appellate court rejected a document—which the lawyer claimed he received seven months after the trial from an anonymous source—in which his deceased
MCLE Test No. 179

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

1. The fundamental rules governing conflicts of interest are set forth in Rule 3-310 of the California Rules of Professional Conduct.
   True. False.

2. A lawyer must obtain informed written consent to a conflict of interest from all members of a class, not just the representative plaintiffs.
   True. False.

3. When the interests of a closely held corporation and its controlling shareholder conflict, the corporation and the shareholder cannot waive the conflict to permit one lawyer to represent them both.
   True. False.

4. When a trial court’s denial of a motion to recuse a prosecutor is supported by the record, the court of appeal should accord deference to the ruling.
   True. False.

5. By making arguments that other parties also support, a lawyer does not assume the representation of those parties.
   True. False.

6. In a business transaction with a client, a lawyer owes no fiduciary duty to his or her client so long as the lawyer complies with Rule 3-300 of the Rules of Professional Conduct.
   True. False.

7. The commission of an act of moral turpitude, dishonesty, or corruption will subject a lawyer to disbarment or suspension.
   True. False.

8. Rule 3-300 of the Rules of Professional Conduct applies to charging liens in hourly fee cases.
   True. False.

9. If a party has waived the attorney-client privilege by freely producing documents to one party, it cannot assert the privilege against another party seeking the same documents.
   True. False.

10. There is no waiver of the attorney-client privilege if production of the privileged documents was coerced.
    True. False.

11. A lawyer may not communicate with a party that the lawyer knows to be represented by another lawyer without the consent of the other lawyer.
    True. False.

12. A lawyer may not communicate directly with a party who has filed a lawsuit in propria persona if the party is being assisted by an attorney who is not of record.
    True. False.

13. A settlement agreement procured in violation of Rule 2-100 of the Rules of Professional Conduct is void, even if the complaining party will not repay the settlement funds.
    True. False.

14. By making arguments that other parties also support, a lawyer does not assume the representation of those parties.
    True. False.

15. A court can punish misconduct by an out-of-state lawyer.
    True. False.

16. It is unethical for a lawyer to take the default of a party known to be represented by another lawyer.
    True. False.

17. The State Bar’s Ethics Hotline is a source of legal advice, not just a research service.
    True. False.

    True. False.

19. If a contingency fee agreement complies with Business and Professions Code Section 6147, an amendment to the agreement does not need to meet the requirements of the statute.
    True. False.

20. A lawyer can recover fees on a quantum meruit theory if the fee agreement with the client did not comply with Rule 2-200 of the Rules of Professional Conduct.
    True. False.

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client supposedly acknowledged that the lawyer did not represent her in the loan transaction. The court chastised the lawyer for failing to disclose his conflict of interest to his client, thereby “bring[ing] financial harm to his client, institutional harm to his profession, and catastrophic harm to himself.”19 However, the court ignored Rule 3-310 of the Rules of Professional Conduct, in which informed written consent, not just disclosure, is required. Moreover, under the circumstances, not even consent would have cured the conflict.

**Motions to Recuse Prosecutors**

In criminal prosecutions, Penal Code Section 1424 authorizes the court under certain circumstances to recuse a prosecutor because of a conflict. During 2008, the California Supreme Court issued three significant opinions on motions to recuse prosecutors pursuant to Section 1424. In two of them, Haraguchi v. Superior Court20 and Hollywood v. Superior Court,21 the court considered the extent to which prosecutors may risk recusal by engaging in extracurricular activities.

Haraguchi22 involved a deputy district attorney who routinely prosecuted defendants accused of committing rape. The attorney was the author of a novel titled *Intoxicating Agent*, an account of the rape of an intoxicated person. The novel features the efforts of a heroine—an intrepid deputy district attorney modeled on the author—to bring the rapist to justice. Three months before the novel was published, the defendant in *Haraguchi* was charged with raping an intoxicated victim. Claiming similarities between himself and his case and the characters and events depicted in *Intoxicating Agent*, the defendant moved to recuse the deputy district attorney pursuant to Section 1424. He argued that his prosecution by the deputy district attorney could be swayed by his interest in generating publicity for himself and her novel and thus he would be precluded from receiving a fair trial.

In *Hollywood*,23 another deputy district attorney from the same office prosecuted defendant Jesse James Hollywood on charges of kidnapping and first degree murder of a 15-year-old boy. The motive for the crimes appeared to be the bungling by the victim’s older brother of a drug deal. While Hollywood was on the lam, the deputy district attorney helped filmmaker Nick Cassavetes make *Alpha Dog*, a movie based on the crimes. The prosecutor gave the filmmaker a copy of his trial notebook, transcripts of testimony from the previous trials, contact information for witnesses, police reports, probation reports, and other materials. In his zeal for justice, however, the prosecutor may have gone too far. Disseminating confidential criminal records, such as police reports and probation reports, is unlawful and may constitute a misdemeanor.24 The movie vilified Hollywood. After he was caught, Hollywood moved to recuse the deputy district attorney.

In both *Haraguchi* and *Hollywood*, the trial courts denied the recusal motions, and the appellate courts reversed. In *Haraguchi*, the appellate court reasoned that the prosecutor’s “views of the justice system, as reflected in her novel, were so one-sided as to raise a reasonable possibility she would not exercise her discretion even-handedly, and her interest in promoting her book presented a conflict so great it was unlikely that the defendant could receive a fair trial.”25 In *Hollywood*, the appellate court commented that “[i]n this case of first impression, we should not give our imprimatur to [the prosecutor’s] conduct or embolden other prosecutors to assist the media in the public vilification of a defendant in a case which is yet to be tried.”26

However, in both cases, the California Supreme Court reversed, because the appellate courts failed to accord sufficient deference to the trial court findings.27 In *Haraguchi*, the supreme court noted that although there was sufficient evidence in the record upon which a trial court could have found that the novel created a reasonable possibility that the deputy district attorney would have handled the defendant’s prosecution differently, the trial court found otherwise—and its findings also were supported by the record.28 According to the court, “That a prosecutor may pursue an independent writing career does not alone create a conflict with the public interest and disqualify her from future prosecutions, absent proof her writings create a material conflict in a particular case.”29

In *Hollywood*, the court noted that “[c]ertainly, a case might arise in which a trial court could order recusal based on the prosecution’s attempt to manipulate the prospective jury pool by disseminating inflammatory portrayals of the defendant.”30 But substantial evidence supported the trial court’s findings that the deputy district attorney wanted to facilitate Hollywood’s capture and portray his character as accurately as possible. Still, the court had stern words for the prosecutor:

This is not to say that [the prosecutor] should escape censure. We find his acknowledged actions in turning over his case files without so much as an attempt to screen them for confidential information highly inappropriate and disturbing. The trial court made no findings as to whether this omission in fact resulted in the illegal or unethical disclosure of confidential documents, and we certainly are not situated to do so here. If it did result in such a disclosure, sanctions are available, as are authorities whose function it is to pursue those sanctions.31

For these and other similar situations, the district attorney’s office has the authority to investigate and prosecute illegal conduct, and the State Bar has the authority to investigate and prosecute unethical conduct.

Last year the supreme court also had an opportunity to consider whether a prosecutor’s advocacy of a victim’s rights may create a conflict of interest requiring recusal. In *People v. Superior Court (Humberto S.*),32 the prosecutor filed a motion to quash a defense subpoena for the victim’s medical and psychotherapy records. When the motion was not granted, the prosecutor filed a writ petition with the court of appeal and moved for the appointment of a guardian ad litem for the victim. With these actions, had the prosecutor undertaken the representation of the victim? No, the supreme court concluded, and therefore the trial court had abused its discretion in recusing the prosecutor because of a conflict. By making arguments that others also support, “the prosecution does not...assume representation of those third parties any more than an amicus curiae whose interests align with a party represents that party by submitting arguments that support its position.”33 The court noted, however, that “the persistent, bad faith use of litigation tactics lawful in and of themselves might in some circumstances evidence an underlying conflict that renders a fair trial unlikely and warrants recusal....”34

**Business Transactions with a Client**

Rule 3-300 of the Rules of Professional Conduct, “Avoiding Interests Adverse to the Client,” has long been a trap for lawyers who confuse their role as a professional adviser to their clients with the role of business partner. The rule prohibits a member of the bar from entering into a business transaction with a client or “knowingly acquire[ing] an ownership, possessory, security, or other pecuniary interest adverse to a client” unless 1) the terms are fair and reasonable to the client, 2) the client has been advised in writing of the terms and of the right to seek advice from an independent lawyer, and has been given an opportunity to do so, and 3) the client consents in writing. Even when a transaction is not governed by the rule, however, lawyers must meet fiduciary duties to their clients, as the State Bar Court ruled in an unpublished decision, *In the Matter of Clifford Lee Casey*.35

In that case, an 80-year-old woman retained attorney Casey to file an unlawful
detainer action when the woman’s tenants fell behind in their rent of a Palm Springs condominium. Casey’s client continued to experience problems managing the condominium, so Casey arranged for her to sign a grant deed conveying the property to two new owners—a company he represented and his minor son. The client remained liable on the deed of trust, which was not canceled or reconveyed to her, and never received a promised $500 reimbursement for taxes she had paid.

The client sued Casey, incurring legal fees of at least $67,000, and won a judgment of $1 but not legal possession of the condominium. The State Bar filed disciplinary charges against Casey and, after a hearing, the judge recommended three years’ probation. Casey appealed, and the three-judge review panel concluded that the lawyer did not violate Rule 3-300 because he had not acquired a pecuniary or financial interest in his client’s property since he was neither a party to the transaction nor a third-party beneficiary. However, the court concluded Casey had significantly harmed his financially and emotionally vulnerable client and was guilty of moral turpitude under Business and Professions Code Section 6106. The court reached this result because Casey had 1) failed to inform his client that she would no longer have any interest in the condominium but would remain on the deed of trust and would continue to receive the tax bills, 2) failed adequately to document the transaction, and 3) had a conflict of interest due to his divided loyalties to her, his corporate client, and his son. The panel was particularly troubled by Casey’s insensitivity, in his opening brief, that “it is nice to protect little old ladies, but it is very common that many people use the age of the client as a ploy to win lawsuits.” In a second pyrrhic victory for the long-suffering client, the panel recommended actual suspension for Casey in addition to probation, though no restitution was required beyond the $500 tax payment.

A challenge to lawyers’ compensation based on an alleged violation of Rule 3-300 was rejected in Shopoff & Cavallo LLP v. Hyon.36 After lengthy litigation involving five successive teams of lawyers for the prevailing plaintiff, the lawyers sought their contingent fees from the multimillion-dollar settlement through an interpleader action. Faced with fees totaling 48.5 percent of the recovery, the client sought to evade payment by arguing that the lawyers had violated Rule 3-300. They did so, according to the client, by acquiring attorney’s liens on the proceeds without complying with the disclosure and consent requirements of the rule. The First District Court of Appeal rejected this argument, noting that while the California Supreme Court had applied Rule 3-300 to charging liens in hourly fee cases in Fletcher v. Davis,37 it had not done so for contingent fee cases, and even if the liens were unenforceable, the underlying fee agreements remained valid and enforceable.38

**Attorney-Client Privilege and Work Product**

In a case now on review by the supreme court, the Second District Court of Appeal denied a petition for extraordinary relief by a client who sought to prevent production of an opinion letter from its lawyers. In Costco Wholesale Corporation v. Superior Court,39 a purported wage and hour class action, the plaintiffs moved to compel production of a 22-page opinion letter prepared at Costco’s request by its outside employment counsel at Sheppard Mullin. The opinion letter reflected the lawyer’s factual investigation, including interviews of company employees, as well as the lawyer’s legal research and expertise regarding wage and hour law. Costco asserted the protection of the attorney-client privilege and work product doctrine for the letter. In response, the plaintiffs argued that the letter was discoverable because Costco had waived the privilege by placing its knowledge and expectations regarding the managerial tasks performed by employees at issue—and this was based on its counsel’s input.

Over Costco’s objection, the superior court ordered the company to produce the letter for in camera inspection by a discovery referee. The referee redacted the letter to remove those parts she believed were protected by the privilege or work product doctrine and concluded that the remaining content was obtained by the lawyer “in her role as fact-finder rather than attorney, a role that could have been performed by a non-attorney.”40

This finding trivializes the importance of a lawyer’s factual investigation. Moreover, it suggests that whenever a court decides in hindsight that a particular task could have been performed by a nonlawyer, the client should lose the protection of the privilege and the work product doctrine.

The superior court ruled that Costco had

The defendant paid a significant sum in settlement that the plaintiff did not want to give back. The plaintiff wanted “to both keep the money and maintain the war.” If the plaintiff had returned the settlement proceeds, no doubt a more appropriate remedy would have been to void the settlement agreement.

The Regents of the University of California v. Superior Court,44 the plaintiffs sued a group of energy suppliers, alleging they unlawfully inflated the retail price of natural gas in California between 1999 and 2002. The defendants were also the subject of an investigation by a federal Corporate Fraud Task Force composed of the U.S. Department of Justice, the Federal Energy Regulatory Commission, the Commodity Futures Trading Commission, and the Securities and Exchange Commission. At the time, it was the Justice Department’s policy to con-
sider a corporation’s willingness to waive the attorney-client privilege when determining whether it would instruct. All the defendants waived the privilege and produced documents in response to government subpoenas.

The plaintiffs moved to compel production of the same documents. They relied on McKesson HBOC, Inc. v. Superior Court— which held that when a holder of the privilege waives it with respect to one party, the holder cannot assert the privilege against others—and Evidence Code Section 912(a), which provides that a privilege is waived “if any holder, without coercion, has disclosed a significant part of the communication...” The superior court denied the motion, and the appellate court affirmed, finding that the defendants had produced the documents to the government because they believed there would be severe regulatory or criminal consequences if they were labeled as uncooperative by the government. Therefore, according to the appellate court, no waiver occurred under Section 912(a) because the production of the privileged documents was coerced by the federal government’s policies.

**Contact with a Represented Party**

Rule 2-100 of the Rules of Professional Conduct provides that when a lawyer represents a client, the lawyer may not communicate directly or indirectly about the subject of the representation with a party the lawyer knows to be represented in the matter by another lawyer, unless the client’s lawyer has the consent of the other party’s lawyer. What happens when a litigant appearing in propria persona uses shadow counsel? What should be done if a lawyer violates Rule 2-100? How does Rule 2-100 affect criminal investigations? Courts addressed these issues during 2008.

In McMillan v. Shadow Ridge at Oak Park Homeowner’s Association, the plaintiff for a time pursued her claims in propria persona with the assistance of a lawyer who wrote a letter to defense counsel stating that he would defend depositions that had been scheduled. When defense counsel contacted the plaintiff directly to give notice of his intent to file an ex parte application to compel the depositions of the plaintiff’s expert witnesses, the plaintiff moved to disqualify defense counsel for violating Rule 2-100. The Second District Court of Appeal held that the trial court did not abuse its discretion in denying the motion. The court stated that the plaintiff “has every right to be assisted by an attorney not of record, but neither she nor the assisting attorney could unilaterally limit the ability of opposing counsel to confer with the attorney of record. As [the plaintiff] was at all times relevant the attorney of record, [opposing counsel] was duty bound to recognize her as such and to treat her accordingly.” With respect to ethical boundaries, the court noted that “a bright line test is essential. As a practical matter, an attorney must be able to determine beforehand whether particular conduct is permissible; otherwise, an attorney would be uncertain whether the rules had been violated until...he or she is disqualified.”

A party in a case is either represented by counsel or not. If the party is not represented, opposing counsel may communicate directly with him or her without violating Rule 2-100. In Myerchin v. Family Benefits, Inc., and United States v. Carona, courts concluded that lawyers violated Rule 2-100. In Myerchin, the defendant’s lawyer, who had known the plaintiff for many years, left a voicemail message for the plaintiff after the plaintiff filed his lawsuit. In it, the lawyer said, “I am trying to help you and your attorney doesn’t know what he is doing and is just ripping you off and will just run up a big bill...Your only chance to settle is to deal with me.” The plaintiff then signed a settlement proposal that the defendant’s lawyer sent to him without consulting with his own lawyer.

In Carona, while a grand jury was investigating possible corruption within the Orange County Sheriff’s Office, a government lawyer wired one of the target defendant’s cronies, armed him with phony subpoena documents intended to trick the target defendant into believing that the crony was about to testify before the grand jury, and sent him to talk with the target defendant with the hope of soliciting evidence to support a charge of obstruction of justice. The government lawyer knew at the time that the target defendant was represented by counsel.

Not surprisingly, the courts in Myerchin and Carona found that the lawyers violated Rule 2-100. Indeed, the courts wrestled more with the appropriate remedy for the violations.

In Myerchin, the Fourth District Court of Appeal agreed with the trial court that notwithstanding the ethical violation, the settlement agreement was still enforceable. This is not a surprising result given the circumstances. The defendant paid a significant sum in settlement that the plaintiff did not want to give back. The plaintiff wanted “to both keep the money and maintain the war.” If the plaintiff had returned the settlement proceeds, no doubt a more appropriate remedy would have been to void the settlement agreement.

In Carona, U.S. District Court Judge Andrew Guilford denied a defense motion to suppress the tape-recorded statements. In doing so, the judge ruled that “the harm caused by suppression is too high a price to pay” and “[t]he State Bar of California has a very effective system for disciplining and deterring attorney misconduct.”

**Lawyers Behaving Badly**

Attorney Anthony Pagkas was sued for malpractice after a default judgment of $730,466 was rendered against his client, Mumbert, by the plaintiff, Styles. When Mumbert appealed the judgment in Styles v. Mumbert, Pagkas displayed the kind of initiative that had been sadly lacking in his representation of his former client and bought Style’s rights to the judgment for an undisclosed sum. He then sought leave of court to substitute himself as respondent in the appeal “to offset any [future malpractice] award against him.”

The Sixth District Court of Appeal denied the motion, holding that as Mumbert’s former lawyer, Pagkas continued to owe his client fiduciary duties, including a duty of confidentiality. The appellate court rejected Pagkas’s argument that he was entitled to reveal confidences to defend himself because he was distinguished between the malpractice action and the case in which the lawyer was seeking to step into the position of Mumbert’s adversary. Unimpressed by Pagkas’s ingenuity, the court held that Pagkas had “violated a myriad of ethical duties” by buying an interest in the judgment against his former client and sanctioned both Pagkas and his lawyer for making a mockery of the Rules of Professional Conduct.

In Sheller v. Superior Court, a Texas lawyer admitted pro hac vice as lead counsel in a class action against Farmers New World Life Insurance Company and Farmers Group, Inc., was sanctioned by the Los Angeles Superior Court when he sent out an advertising flyer to 350 policyholders, seeking additional class representatives. The flyer stated falsely that “Farmers may have given you misleading information about this lawsuit” and that if a policyholder was accepted as a class representative, “you are paid for your time in an amount set by the judge.” After the lawyer’s explanations proved contradictory and inadequate, he was formally reprimanded and ordered to pay Farmer’s attorney’s fees of $95,009. Writing for the Second District Court of Appeal, Justice H. Walter Croskey agreed that the flyer was “completely false” but held that the superior court lacked authority to impose the sanctions, which were vacated. However, because a court has the inherent power to revoke an attorney’s pro hac vice admission, the appellate court remanded the case for further proceedings.
aside a default judgment as an abuse of discretion in Fassey v. Permatex, Inc.64 Three weeks before the statute of limitations expired, the plaintiff filed a personal injury action. Despite being provided with the address of the agent for the defendant, Permatex, by the legal department of the parent company of Permatex for service of process, the plaintiff’s lawyer, Robert J. Hooy, did not serve the lawsuit until after the time set forth in the California Rules of Court and the issuance of the case management order by the superior court. The complaint was forwarded to the defendant’s insurer, but it failed to file a responsive pleading. Without further notice to Permatex or its parent, the plaintiff’s lawyer filed a request for default and, 13 days later, obtained a default judgment for $236,500. Within days, Permatex learned of the judgment and asked Hooy voluntarily to set it aside, but he refused. Permatex filed a motion for relief from default, but it was denied in a four-word order. The court of appeal reversed, noting that there was no lack of cooperation from the defense side: “No deception. No duplicitousness. No stonewalling. No evasion. No disregard of any warning. In fact, no warning.”65 It concluded that the plaintiff’s counsel had an ethical obligation to warn Permatex before he took the default, quoting Weil and Brown’s treatise66 and the California Attorney Guidelines of Civility and Professionalism: “An attorney should not take the default of an opposing party known to be represented by counsel without giving the party advance notice.”67

Lawyer Joanna Mendoza and her clients were jointly and severally sanctioned $43,678 for violating a protective order by disclosing trade secret information to third parties. In Wallis v. PHL Associates, Inc.,68 an attorney for the opposing parties filed a declaration with 800 pages of attached trade secret documents. Although the declaration plainly stated that it was filed under seal and was sent to the court in a sealed envelope, the documents appeared in a court file available to the public. Learning of the public availability of the trade secret documents, Mendoza arranged for her clients and third parties to copy them. After being sanctioned, they appealed. The Third District Court of Appeal affirmed, holding that their argument that the appearance of the documents in the court file allowed them to disclose the trade secrets was frivolous, and their disclosure of the information was in bad faith.

In her defense, Mendoza claimed that she had spoken to someone at the State Bar’s Ethics Hotline, who advised her that her paramount duty was to tell her clients about the public availability of the trade secret information. Taking this step, she argued, showed her good faith. The appellate court concluded, however, that Mendoza did not discuss with the person at the Ethics Hotline that she was subject to a protective order, which she was bound to obey, and this supported the conclusion that she had acted in bad faith. Moreover, as the court noted, the Ethics Hotline is a confidential research service, “not a source of legal advice.”69

Getting Paid
Several legal authorities govern fee agreements. Business and Professions Code Section 6148 sets forth certain requirements for most noncontingency fee agreements.70 Business and Professions Code Sections 6146, 6147, and 6147.5 contain requirements applicable to most contingency fee agreements. Rule 2-200 of the California Rules of Professional Conduct applies to agreements between lawyers to split fees. In 2008, courts analyzed these authorities and reinforced the general principle that lawyers who fail to comply with applicable rules risk some or all of their fees.

In Stroud v. Tunzi,71 the Second District Court of Appeal held that a lawyer may not enforce the terms of an amendment to a contingency fee agreement unless the amend-
concluded in strongest Vin, the Fourth District Court of Appeal firm. In 2008, in a matter of first impres-
sion, the Fourth District Court of Appeal concluded in Strong v. Beydoun that a lawyer could not even assert a quantum meruit claim against a client because the fee agreement failed to comply with Rule 2-200. In Strong, the plaintiff, a lawyer, entered into a written fee-splitting agreement on a contingent fee case with another lawyer. The plaintiff agreed to assist the other lawyer in prosecuting a case on behalf of two clients. After the other lawyer promised the plaintiff that he would get the clients’ signatures on the fee-splitting agreement, the plaintiff began to work on the matter. The clients never signed the agreement. As a result, the fee-splitting agreement violated Rule 2-200. After about a year, the other lawyer terminated the plaintiff’s services. Thereafter, the clients settled, and the other lawyer collected the contingency fee. Notwithstanding the work that the plaintiff had devoted to the case, the plaintiff received nothing. She sued the clients and her former cocounsel. The trial court sustained the former clients’ demurrer to her complaint, and the Fourth District Court of Appeal affirmed: “It makes no sense to allow an attorney whose only connection to the client is through an unenforceable fee-sharing agreement to recover fees directly from that client. [The plaintiff’s] recourse is against [the other lawyer].”

Other rules may also apply, as illustrated in Mark v. Spencer. Two lawyers and their client agreed in writing that all fees awarded by the court to the lawyers for prosecuting a class action with their client as the class representative would be evenly split between them. The agreement complied with Rule 2-200, but the lawyers failed to disclose the agreement to the court when they moved to approve the class action settlement, as required by California Rule of Court 3.769(b). Based on their fee declarations, the court handling the class action awarded $401,000 in fees to one lawyer and $76,000 to the other. The one receiving the lower amount of fees did not know about Rule of Court 3.769(b) and deferred to his cocounsel, who was more experienced in class action litigation. What price did he pay for his lack of experience? His cocounsel refused to honor the fee-splitting agreement. The lawyer receiving the lower award sued but without success.

In affirming a dismissal of the lawsuit on demurrer, the Fourth District Court of Appeal wrote, “We are not persuaded to protect [the lawyer’s] interest in the fee splitting agreement at the expense of the…class members.” Experience comes at a price.

When a client disputes a fee, the client has the option to force his or her lawyer to arbitrate the fee dispute through a local bar association pursuant to the Mandatory Fee Arbitration Act (MFAA). Under the MFAA, the fee award becomes final if neither party rejects it and requests a trial de novo within 30 days after the mailing of the appropriate statutory notice of the award. In Perez v. Grajales, a client was awarded $124,000 against her lawyer after an MFAA arbitration. The lawyer filed a lawsuit challenging the award and requested a trial de novo within 30 days, but ultimately his action was dismissed for failure to prosecute.

What effect did the involuntary dismissal have on the lawyer’s challenge to the MFAA award? Analyzing this issue of first impression, the Sixth District Court of Appeal concluded that the involuntary dismissal constituted a repudiation of the lawyer’s challenge to the award, thereby empowering the client to petition to confirm the award—even
though the client’s cross-complaint also had been dismissed for failure to prosecute. The court noted that “[a]llowing a party to avoid the adverse consequences of an MFAA arbitration award by failing to prosecute the case to a de novo trial would ‘produce[] absurd consequences and promote[] mischievous lawyering.’”

Once an MFAA award in favor of a client becomes final, it behooves the lawyer to pay it. In fact, as illustrated in Chandler v. State Bar, if a lawyer fails to satisfy a final monetary award in favor of a client under the MFAA, the State Bar can initiate proceedings before the State Bar Court to place the lawyer on inactive status. Chandler also illustrates that lawyers cannot object properly to an MFAA award by simply filing a lawsuit seeking the reasonable value of their services. Lawyers must specifically object to the award and request a trial de novo.

Revision of the Rules of Professional Conduct

The Commission on the Revision of the Rules of Professional Conduct continued its multi-year task of revising California’s ethics rules by publishing new rules for public comment. It also held regular meetings around the state and will continue to do so in 2009. The public is invited to attend.

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3 Milberg Weiss Co-Founder Sentenced to 2-1/2 Years for Kickback Schemes, 24 Laws. Man. on Prof. Conduct (ABA/BNA) 295 (June 11, 2008).
9 ABA Stands Pat on Lateral Lawyer Rules, ABA J., Aug. 12, 2008.
12 Sharp v. Next Entm’t, Inc., 163 Cal. App. 4th 410 (2008). In January 2009 the parties reached a settlement in which the defendants agree to pay the plaintiffs more than $1.5 million to resolve their claims of unpaid overtime. See http://www.law.com/spip/spip/4/PubArticleNLJ

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13 Sharp, 163 Cal. App. 4th at 433.
14 Id. at 431-32, 433.
15 Id. at 432-33.
17 Id. at 214.
19 Id. at 158.
22 Haraguchi, 43 Cal. 4th 706.
23 Hollywood, 43 Cal. 4th 721.
24 See, e.g., PENAL CODE §§1203.5, 11105, 11140-11144.
25 Haraguchi, 43 Cal. 4th at 711.
26 Hollywood, 43 Cal. 4th at 727.
27 Haraguchi, 43 Cal. 4th at 711; Hollywood, 43 Cal. 4th at 725.
28 Haraguchi, 43 Cal. 4th at 717.
29 Id.
30 Hollywood, 43 Cal. 4th at 732.
31 Id. at 735.
32 People v. Superior Court (Humberto S.), 43 Cal. 4th 737 (2008).
33 Id. at 725.
34 Id. at 747.
40 Id. at 498.
41 D. I. Chadbourne, Inc. v. Superior Court, 60 Cal. 2d 723 (1964).
43 Costco, 161 Cal. App. 4th 725.
46 Regents, 165 Cal. App. 4th at 677-78.
47 Id. at 683-84.
48 CAL. RULES OF PROF’L CONDUCT R. 2-100(A).
50 Id. at 961.
51 Id. at 966.
54 Myerchin, 162 Cal. App. 4th at 1531.
55 Id. at 1533.
56 See also McMillan, 165 Cal. App. 4th at 968 (“The court’s goal is not to impose a penalty, as the propriety of punishment for violation of the Rules of Professional Conduct is a matter within the purview of the State Bar, not of a court presiding over the affected case. Instead, what the court must do is focus on the appropriate remedy for whatever improper effect the attorney’s misconduct may have had in the case before it.”) (emphasis in original) (citations omitted)).
58 Id. at 1166.
59 Id. at 1169.
60 Id. at 1170.
62 Id. at 1703.
63 Id. at 1718.
65 Id. at 701.
69 Id. at 900.
70 Section 6148 generally requires that noncontingency fee agreements be memorialized in writing (signed by the lawyer and the client). The agreement must include 1) a disclosure of the fees and charges applicable to the case, 2) a description of the services to be rendered, and 3) the respective duties of the lawyer and the client. BUS. & PROF. CODE §6148(a). A fee agreement that fails to satisfy all the applicable requirements is voidable at the client’s option, but the lawyer is nevertheless entitled to recover a reasonable fee for any work performed. BUS. & PROF. CODE §6148(c).
72 Section 6147 requires that a contingency fee agreement must be memorialized in a writing (signed by the lawyer and the client). The agreement must include 1) a disclosure of the contingency rate, 2) an explanation of how disbursements will be handled, 3) a statement regarding what extent, if any, the client could be required to pay any compensation to the lawyer for related matters falling outside the contingency fee, and 4) a disclosure that the fee is not set by law but rather is negotiable (unless a certain limited exception applies). BUS. & PROF. CODE §6147(a). A contingency fee agreement that fails to satisfy all the applicable requirements is voidable at the client’s option, but the lawyer is entitled to recover a reasonable fee for any work performed. BUS. & PROF. CODE §6147(b).
75 Strong, 166 Cal. App. 4th at 1404.
77 Rule 3.769(b) of the California Rules of Court provides: “Any agreement, express or implied, that has been entered into with respect to the payment of attorney’s fees or the submission of an application for the approval of attorney’s fees must be set forth in full in any application for approval of the dismissal or settlement of an action that has been certified as a class action.”
78 Mark, 166 Cal. App. 4th at 229.
79 Mandatory Fee Arbitration Act, BUS. & PROF. CODE §56200 et seq.
83 Id. at 502 (quoting Herbert Hawkins Realtors, Inc. v. Milheiser, 140 Cal. App. 3d 334, 339-40 (1983) (footnote omitted)).
84 Chandler, 2008 WL 901865.
85 For the proposed new rules and a schedule of the commission’s public meetings, see http://www.calbar.ca.gov.
ON SATURDAY, MARCH 7, the Los Angeles County Bar Association, the Barristers, the judges of the Los Angeles Superior Court, and the Los Angeles Daily Journal will present a program offering a general overview of the Los Angeles Superior Court. The presenters—Phillip C. Baker, Julie Bronson, Steven R. Cerveris, John J. Collins, Judge Emilie H. Elias, Robert S. Fink, Tom Girardi, Judge Aurelio Muñoz, Linda Rice, Jerome L. Ringler, Linda Star, and Alexander H. Williams III—will share valuable ideas for successful pretrial and trial techniques and discuss common pitfalls to avoid in the courtroom. The first hour will involve court administration issues and alternate dispute resolution. Among the topics to be covered during the afternoon session are opening statements, voir dire, cross-examination, and final arguments. Interested lawyers, law students, and paralegals are encouraged to attend. The program will include segments on basic courthouse orientation, ADR, courtroom demeanor, law and motion, writs and receivers, and discovery. In addition, prominent trial lawyers will present parts of a mock trial based upon a medical malpractice hypothetical. Continental breakfast, breaks, and lunch will be included. The program will take place at the Los Angeles Superior Court, 111 North Hill Street, Downtown. Parking is available at no charge at lot 17 (entrance is on the west side of Olive Street just south of First Street). This program will begin at 8:30 A.M. and end at 3:45 P.M. The deadline for advanced payment is noon on February 23. The registration code number is 010340. The prices below include the meals.

$55—CLE+PLUS members
$90—payment before noon on February 23
$125—all at-the-door registrants
6 CLE hours

On Wednesday, March 4, from 11:30 A.M. to 12:30 P.M., the Los Angeles County Bar Association and the Small and Solo Division will present a webinar, or online seminar, on computer forensics. Alexander H. Lubarsky will show how today’s computer forensic technology can be applied to aid in electronic discovery as well as to find the hidden or deleted e-mail message or file that can help you win your case. This program will discuss the definition and evolution of computer forensics and how cutting-edge law firms are harnessing forensic technology to give clients a substantial advantage in civil and criminal litigation. An overview of a key computer forensics tool will be demonstrated. Those who attend will learn how to best select a computer forensic expert for data analysis and trial testimony. Registration for this program closes on March 2. Early registration is required because of the special nature of the program. Those who enroll must provide an e-mail address prior to the program. The registration code number is 010159. The prices below include the meal.

$15—CLE+PLUS members
$55—Small and Solo Division members
$90—LACBA members
$120—all others
1.5 CLE hours

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.
“NEWCOMER AIMS TO DETHRONE ASSEMBLYMAN.” That’s what the headline read in the October 30, 2008, edition of Easy Reader, a South Bay weekly newspaper. The thoughts racing through my mind when I read the article that morning—a mere five days before the most momentous political election in my lifetime—were exhilarating, despite the fact that in the previous nine months, I couldn’t recall a single night in which I had slept more than five hours.

The year 2008 was an incredible one for American politics. People were engaged in, and captivated by, the political process at a level most of us had never before experienced. Understandably most people were enraptured by the presidential election. Personally, I was caught up in a different, less-talked about race. I was the newcomer aiming to dethrone the incumbent in my state assembly district.

I decided to run for office because I had grown weary of the elected officials who are in leadership positions but who fail to lead. I believe that we have to elect new leaders who are capable of, and committed to, making life better for all of us, instead of mere politicians who care about us only when it is time for their reelection. I wrestled long with the decision to run for office. It was a difficult decision because I had worked so hard over the past nine years to become a good lawyer, build my own book of transactional entertainment clients, and establish myself as a candidate for partnership at the large firm where I worked. Campaigning for a political office would likely mean walking away from all of that. Besides, there was no guarantee that I’d even win my election. Yet, I could not shake the desire that I had to try to make a difference as an elected official.

In the end, I decided that the promise of security would not be worth a lifetime of regret. As Helen Keller noted, “Security is mostly a superstition. It does not exist in nature, nor do the children of men as a whole experience it. Avoiding danger is no safer in the long run than outright exposure. Life is either a daring adventure or nothing.” I chose the life of adventure. I didn’t choose it because I’m a thrill seeker, but because I believe that cautious and careful people never bring about reform. Restlessness and discontent, as Thomas Edison noted, are the first necessities of progress. (Of all the things I worried about losing, only the chance for partnership at my firm actually dissolved. I left the firm after the primary election to focus full time on my campaign.)

Of course, the reason some people choose the path of least resistance is, well, because there is less resistance. Campaigning for public office epitomizes the epic struggle of David against Goliath—and his three brothers. There’s plenty of resistance. As a practicing lawyer, I have been no stranger to grueling work and long hours. Campaigning for a state office, however, is another level altogether. There are tremendous demands on the candidate, particularly a challenger. The candidate is ultimately responsible for fund-raising; obtaining endorse-

 Campaigning for public office epitomizes the epic struggle of David against Goliath—and his three brothers.

ments; coalition building among voters and centers of influence; developing a political strategy; communicating the campaign message to voters, donors, elected officials, organizations, and the media; organizing the campaign; and getting out the vote. Moreover, all these tasks must be timed to occur with the precision of a classical symphony. That is the campaign environment every candidate must face, but each campaign has its unique features. My own race was particularly challenging for two reasons. First, I was running against an incumbent. Incumbents generally have some measure of name recognition and a tremendous advantage when it comes to campaign cash, which makes it extremely difficult to defeat them. The reelection rate for incumbents is well beyond 90 percent. The problem for the challenger is convincing the voters that the current guy is doing such a bad job that his contract should not be renewed and convincing them that the challenger is more qualified for the position. Assuming the candidate has the goods, it still takes an engaged electorate that is paying attention to the race and sufficient financial resources to get the message out in order to prevail on Election Tuesday.

Second, I am a conservative Republican who campaigned in an election cycle that greatly favored Democrats. The biggest challenge is that a down-ticket candidate has only a very limited ability to define what it means to be a member of his or her party. To a large extent, the candidate is defined by the party’s elected officials, the media, and the national campaigns. Consequently, unless the voters are paying close attention to the race, the candidate must live with an image created by others.

I worked as hard as I possibly could on my campaign. The campaign hosted 14 major community events. I built and managed a volunteer base of more than 150 people who walked 30,000 homes, made countless phone calls, set up appointments, delivered lawn signs, and stuffed and licked envelopes. Despite all these efforts, I did not prevail on Election Day. But I prevailed in every other way, and I earned some 62,000 votes in the process. You can bet I’ll be back again.

More young lawyers need to opt for the life of adventure. Pearl Buck once commented that “the young do not know enough to be prudent, and therefore they attempt the impossible—and achieve it, generation after generation.” We need more young people who are willing to take the risk to do impossible things. Who knows? We just might accomplish them. I will certainly keep trying.

Thomas H. Vidal is an entertainment lawyer in Los Angeles.
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