

Editor's Introduction

So you cleaned house on your defaulted loans and now have one or more judgments. Now is as good a time as any to convert your judgment into money by utilizing one or more of several available post-judgment enforcement procedures. **Bob Benjy's** and **Chun Hsu's** judgment collection article is a useful primer for judgment creditors seeking to collect.

For those of us who are simply minding our collateral, **Carol Robertson's** article on the Los Angeles REAP program is a valuable summary of how, when and why the city is empowered to intercept your collateral's income stream at your expense. The article familiarizes readers with REAP and provides practical advice for how lenders may avoid the unpleasant consequences.

Hal Goldflam's article analyzes a recent California Court of Appeal opinion concerning the intersection between check cashing businesses and fraudulent employee endorsement of business checks. His article summarizes the court's opinion and educates readers on the liability exposure of first-level depository banks when accepting business checks presented for deposit for potential endorsement fraud. ▀



Money Judgments Are Not for Hanging on Walls

By BOB BENJY and CHUN HSU

After a protracted and contentious legal battle, a lender has prevailed on its breach of promissory note claim and obtained a money judgment against a defaulted borrower for the full amount of the debt, plus all legal fees expended. However, because a judgment is not self-enforcing and many judgment debtors do not voluntarily pay the judgment, it is incumbent upon the judgment creditor to take enforcement actions against the assets of the judgment debtor to satisfy the judgment. Luckily, California law provides a multitude of post-judgment procedures to assist judgment creditors to enforce and collect money judgments in California.

The key to enforcing a judgment is identifying the judgment debtor's assets to attach and knowing where those assets are located. To that end, it is pru-

dent for a lender to collect the borrower's financial and credit information during the ordinary course of the lending relationship.

However, if the lender has insufficient information regarding a borrower's assets and financial condition for judgment collection purposes, the judgment creditor may employ various post-judgment means to identify and locate the assets of a judgment debtor to attach.

Effective post-judgment discovery procedures include judgment debtor's examinations, third-party examinations, and document subpoenas. For instance, upon an application by the judgment creditor, the court may issue an order compelling the judgment

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35 YEARS
of SERVICE

Read This and REAP

The City of Los Angeles' *Constitutional* Taking of Your Collateral

By CAROL A. ROBERTSON

While lenders are generally familiar with condemnation of real property collateral by governmental agencies, they may be less familiar with the ability of a governmental agency to interrupt the income stream from their real property collateral. Lenders who have borrowers that fail to maintain the multi-family rental units they own in habitable condition may find that their collateral (the rents) are diverted into an account controlled by the City of Los Angeles if one or more units are placed into the Real Estate Escrow Program (REAP). REAP is administered by the City of Los Angeles Housing Department (LAHD) and applies to all dwelling units in the City of Los Angeles. "REAP works in conjunction with other enforcement programs to combat substandard housing in Los Angeles and to encourage landlords to comply with the housing code." *Sylvia Landfield Trust v. City of Los Angeles*, 729 F.3d 1189, 1193 (9th Cir. 2013).

The City places properties into REAP when the landlord fails to correct health, safety, or habitability violations on rented, residential property. In addition to a reduction in rental income, once a property is accepted into REAP, the landlord's operating expenses will increase due to repairs which will be mandated under the REAP program. What about selling the rental units to simply get rid of the problem, or refinancing the building to fund the necessary repairs? Once the units are in REAP, the City

of Los Angeles will record a Notice of REAP against the rental property in the real estate records of Los Angeles County, which may impede the sale or refinancing of the property.

The constitutionality of REAP was challenged in *Sylvia Landfield Trust*. In that case, the United States Court of Appeals for the Ninth Circuit affirmed the District Court's dismissal of a complaint brought by four landlords challenging the constitutionality of REAP. The Court of Appeals held, among other things, that: (1) REAP was rationally related to the legitimate governmental interests of repairing and preventing substandard housing; (2) REAP did not violate plaintiffs' substantive due process rights; and (3) that the placement of plaintiffs' properties into REAP did not shock the conscience. See *Sylvia Landfield Trust* at 1196.

Getting into REAP

"REAP deems a residential unit 'untenantable' if it lacks sufficient waterproofing, weather protection, plumbing, gas facilities, water supply, heating facilities, or electrical lighting REAP also mandates that the building and grounds be free of 'debris, filth, rubbish, garbage, rodents and vermin Buildings must have garbage receptacles, and landlords must maintain floors, stairways, and railings in good repair." *Sylvia Landfield Trust* at 1194. Residential rental properties that fail to meet these minimum standards may be involuntarily placed into REAP.

Any Enforcement Agency (i.e., any governmental agency that inspects rental units for compliance with health or safety laws, such as the Department of Health Services) or tenant may refer a rental property or unit to the LAHD for acceptance into REAP if:

The building (or unit) is the subject of one or more orders or notices to comply,

correct or abate a condition or violation issued by an Enforcement Agency.

1. The period in which to comply with the order has expired without compliance.

2. The violation affects the health or safety of the occupants, is subject to the Rent Stabilization Ordinance or the violation results in a deprivation of housing services.

3. When the LAHD receives a referral, it will verify that the period for correcting the violation(s) has expired and will check for any other outstanding orders against the property. The determination will be mailed to the landlord, but the failure of the landlord to receive the notice does not invalidate any subsequent proceedings.

Once a property is accepted into REAP, the owner will be notified of the amount of rent reduction, the date the escrow account will be established, the \$50 per month per unit administrative fee and whether or not the building will be referred for periodic inspections at the owner's expense. The LAHD will mail a notice to the tenants and advise the tenants that they have the choice of paying (reduced) rent into the REAP account or continuing to pay rent to the landlord.

If the violations are such that more than one unit in a building is likely to be impacted, all of the affected units can be placed into REAP (and thus subject to a rent reduction).

Rent reductions are determined according to the severity of the problem and any prior history of placement of other properties owned by the same landlord into REAP. The rent reduction applicable to any unit is determined by adding up all of the percentage reductions in each of the 15 categories of violations, subject to a cap of 50% reduction in monthly rent. However, the 50% cap can be exceeded where the land-



Carol A. Robertson's practice emphasizes commercial lending transactions and workouts of loans secured by real and personal property.

lord owns other properties that were in REAP for more than 12 months and in more extreme cases, the rent reduction may increase to 100%.

Appealing the REAP determination

Once the property is placed into REAP, the landlord has 15 calendar days from the date the notice described above is mailed to submit a written appeal and request a hearing before the General Manager of the LAHD. If no appeal is filed, the property is automatically placed into REAP. Any appeal must be made on the form prescribed by the LAHD and while the appeal is pending, the placement of the property into REAP will be stayed.

The General Manager will serve a notice of the hearing date on the landlord and the affected tenants at least 7 days prior to the hearing. If the appeal is made timely and meets the LAHD's requirements, the General Manager will set a hearing date within 30 days of the LAHD's receipt of a request for a hearing. Landlords, tenants and any Enforcement Agency may attend the hearing and present evidence. A landlord may present evidence that a rent reduction is not appropriate because the substandard conditions and violations were caused by the tenants. The burden of proof is on the landlord. The hearing officer must issue a written decision within 10 working days of the date of the hearing, and may affirm, modify or reverse the determination by the LAHD.

Appealing the Appeal

The landlord, any tenant or the Enforcement Agency may appeal the determination by the General Manager to the Appeals Board within 10 calendar days after receipt of the General Manager's determination. The appeal must state which portions of the determination are being appealed and the basis for the appeal. Enforcement of the parts of the determination being appealed are stayed pending the outcome of the appeal.

Another hearing is scheduled and the owner, tenants and the Enforcement Agency are given five days' notice of the hearing date. The Appeals Board is charged with reviewing any alleged errors or law or abuse of discretion and no new evidence will be entertained unless newly

discovered. The Appeals Board will make a decision within 15 days of the hearing.

What to expect while in REAP

Within five working days after a final decision (i.e., all appeals have been exhausted) that a building or units have been accepted into REAP, the LAHD will open an escrow account.

The LAHD will record a notice with the Los Angeles County Recorder's Office stating that the property has been placed into REAP. This notice will be reflected in any preliminary title search conducted against the property and will cloud title.

The landlord will receive a monthly accounting of the rents paid by the tenants, as well as any permissible deductions from the account, such as the \$50/month per unit administrative fee.

A Case Manager from the LAHD will be assigned and the landlord can anticipate that the scope of any inspections will go beyond the specific violation(s) that triggered placement of the building into the REAP program. Landlords with buildings in REAP can also expect multiple inspections at their expense. The \$50 per month per unit administrative fee will continue to accrue as long as the unit in question is occupied.

While a property is in REAP, a landlord, tenant, Enforcement Agency or a creditor may apply to the General Manager for a release of funds from the REAP account. A withdrawal of escrowed funds may be approved (after a hearing) for the following reasons:

1. To pay for essential services, such as utilities, trash and managerial services.
2. To correct deficiencies in the condition of the property;
3. To the extent legally permissible, by a tenant to repair conditions that affect the tenant's health and safety;
4. To a tenant who has or will relocate;
5. To a tenant who has incurred expenses due to the unit being uninhabitable;
6. In response to a court order; and/or,
7. To satisfy a judgment under L.A. Municipal Code Section 162.09.C.

Funds in the REAP account may be released on shortened notice or without a hearing if necessary to address an imminent threat to the building's oc-

cupants, or to prevent the termination of utilities.

Getting out of REAP

Once all of the violations that triggered the placement into REAP (and any subsequent orders) have been cured, the landlord, the affected tenant or the Enforcement Agency may notify the LAHD that compliance with all orders has been achieved. The landlord may also apply to have the rent reductions lifted on units that are in compliance, even though other units in the same building are still in violation. Any assertions that all violations have been resolved will have to be supported by appropriate inspections, and the LAHD may impose conditions, such as requiring the landlord to prepay the cost of 2 annual property inspections. If the LAHD determines that the landlord has satisfied all outstanding orders and has paid all charges owing for LADWP services, the LAHD may recommend the termination of the REAP account to the Los Angeles City Council.

If the REAP account is terminated by resolution of the City Council, any funds in the account are first used to pay administrative fees and penalties, and then any remaining amounts to the landlord. The landlord will be responsible for any negative balance in the escrow account. While the timeframes for the appeal process are quite specific, it is unclear how long the City Council could take to terminate the escrow account.

Lovely parting gifts

When the REAP account is closed, things should go back to normal, right? Not so, as the landlord stays in the "penalty box" for an additional year. Until a unit is removed from REAP, and for one year thereafter, the landlord may not increase the rent for the current (or any subsequent) tenant. During this same one year period, if a landlord wants to evict a tenant for reasons other than nonpayment of rent, the burden is on the landlord to demonstrate that the eviction is not retaliatory in nature.

What's a lender to do?

Regular physical inspections of the rental units to make sure that the property is being properly maintained according to

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STAYING VIGILANT

The Intersection Between Fraudulently Endorsed Business Checks Presented for Deposit by Check Cashing Businesses and the ‘First Bank’ Rule

By HAL D. GOLDFLAM

Does a bank that receives the deposits of forged endorsement checks from its check cashing service customer (or Money Services Business) potentially have liability to the payee (a business) if the bank's negligence in accepting the checks for deposit contributed to the loss? In a recent decision published by the California Court – *HH Computer Systems, Inc. v. Pacific City Bank* – the court held, yes.

The facts presented in this case are common: An employee of a corporation with responsibility to gather incoming checks made payable to the corporation and deposit those checks into the corporation's bank account (in this case, the corporation's accounting manager), steals some of the incoming checks and takes them to a check cashing service where she forges the signature of one of the officers of the corporation (in this case, nothing more than her "illegible scrawl") and receives hard cash in return. After discovery of the thefts, the corporation fires the employee and, as part of its recoupment efforts, sues not only check cashing services where the dishonest employee took the checks, but the three banks which received the checks from the check cashing services for deposit into those companies' own accounts.

The appeal arose from a judgment of dismissal entered by the trial court after it

sustained a demurrer by the banks to the corporation's complaint. The legal issue presented in this appeal was one of first impression in California: Does the interposition of the check cashing services between (a) the employee who stole the checks and (b) the banks who took the checks from the check cashing companies and credited the accounts of those check cashing companies, relieve the banks of all duty of care under Section 3405 of California's Commercial Code? The Court of Appeal concluded, no. Specifically, the court held that a check cashing service is not a "bank" for UCC Article 3 & 4 purposes, so the defendant banks were the "first banks" to process the forged endorsement checks for deposit and collection. Being "first banks" that received the forged checks for deposit and collection, the banks were "depository banks" having a duty of care under Section 3405 in the processing of those checks to make certain all endorsements were valid.

The court therefore reversed judgment of dismissal allowing the corporation to continue with its claim for negligence under Section 3405, noting that corporation stated a claim for negligence against the banks for allegedly accepting checks payable to a business from a check cashing service without contacting the business to confirm that the transaction was authorized; however, the court also confirmed that under Section 3405, the banks would only liable under a comparative negligence analysis.

Notably, the Court of Appeal stated that its decision "articulated no more of a burden even on *first banks* than they already have. That burden is a light one: (a) It only affects first banks which have check cashing companies as customers, and even then it only

applies (b) to those checks presented by check cashing companies to their own banks which are made out to a business or corporation. . . . And even as to *that* tiny percentage, check cashers and their banks can protect themselves by the simple expedient of the check casher obtaining a written authorization from any business or corporation to whom a check is payable that the business or corporation has authorized a given individual to sign checks on its behalf. . . . In a word, today's decision will not require even depository banks to hire armies of employees to examine each check like something out of Harry Potter's Gringotts. It will require only a minimum level of reasonable care."

In summary, *HH Computer Systems, Inc. v. Pacific City Bank* provides that: (1) check cashing businesses are not *depository* first banks – one does not *deposit* money into a check cashing company; (2) a first-level *depository* bank is included within the ambit of ordinary care envisaged by Section 3405, even if check cashing companies get between the fraudulent employee and the first-level depository bank; and (3) a *depository* bank may liable to a corporate payee of an instrument under Commercial Code section 3405 where the *depository* bank failed to exercise ordinary care in paying an instrument that was fraudulently endorsed by the payee's employee and to the extent the failure to exercise ordinary care contributed to the loss. The court also noted that it was not holding that a "collecting" or "intermediary" bank that is not also a depository bank is within the ambit of ordinary care envisaged by Section 3405 – a non-depository bank has a lesser duty of care than a depository bank. ▀



Hal D. Goldflam is a litigator and his practice emphasizes business, creditors' rights and real estate-related litigation in federal and state courts.

REAP

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code would be the best way to avoid the horrors of REAP, but this is not a practical solution.

When a lender discovers that the multi-family building that is the collateral for its loan has been placed into REAP, the first step would be to meet with the borrower to determine how he/she/it plans to address the deficiencies and how the corrections will be funded. If the borrower is cooperative and amenable to fixing the problems, the lender should monitor the remediation and inspection process to make sure that the landlord is working diligently to cure the violations.

If the borrower is uncooperative or for any reason cannot make the necessary repairs, one possible solution would be to file a motion with the court seeking the appointment of a receiver over the property with the power to make the necessary corrections and negotiate with LAHD to get the property out of REAP. Under Section 564(b)(9) of the California Code of Civil Procedure, a receiver may be appointed where necessary to preserve the property or rights of any party. If appointed, the receiver would be tasked with making sure that the appropriate repairs have been made and guiding the building out of REAP. However, in order to utilize this option, the lender will need to first file suit against the landlord-borrower.

Most well-drafted deeds of trust include provisions: (a) requiring the borrower to maintain the property in tenantable condition, including performing all repairs, replacements, and maintenance necessary to preserve its value; (b) requiring the landlord to comply with laws applicable to the use and occupancy of the property; (c) take action to protect and preserve the property. Accordingly, the fact that a building has been placed in REAP may itself be sufficient grounds for obtaining a receiver. While receivers are expensive, this may be the best way to resolve REAP issues while minimizing the risks to the lender. ■



Bloom



Csato



Welin



Master

NAMES IN THE NEWS

Steven N. Bloom, **Peter Csato** and **Craig A. Welin** were each recognized as 2015 Super Lawyers and **Hemal K. Master** was recognized as a 2015 Rising Star by *Super Lawyer* magazine.

Andrew K. Alper presented at the National Equipment Finance Agreement Conference on the topic of Best Practices in the Leasing and Finance Industry.

Thomas M. Robins III and **Hal D. Goldflam** prevailed at trial on a case where the guarantor raised a sham guaranty defense in reliance upon the original lender's term sheet having required the defendant to form a limited liability company to become the borrower with the defendant acting as guarantor.

Tricia L. Legittino was quoted by *Law 360* in an article concerning *Young v. United Parcel Service Inc.*, a recent U.S. Supreme Court decision concerning the Pregnancy Discrimination Act.

Hemal K. Master gave a presentation entitled "Legal Issues in EB-5 Lending" to the Financial Institutions Committee of the State Bar of California. Hemal was also quoted in an article titled "Four Pitfalls for Foreign Investment in U.S. Real Estate" in *Law 360* on March 11.

Loren R. Gordon was appointed to membership on the Commercial Transactions Committee of the Business Law Section of the State Bar of California.

Bob Benjy gave an audio podcast interview to Thomson Reuters - Legal Current on the issue of the risks and potential issues surrounding mobile payments and banking.

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Money Judgments

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debtor to appear for a judgment debtor's examination to answer questions regarding the judgment debtor's income, assets and other financial condition.

At the examination, the judgment creditor is entitled to ask questions regarding, *e.g.*, the existence, location, amount, value and/or source of the judgment debtor's income and real and personal property, partnership interest, membership interest in limited liability companies, and anything else that may be used to generate proceeds to satisfy the judgment. If any third party is indebted to the judgment debtor in an amount over \$250 or possesses or controls property in which the judgment debtor has an interest, the judgment creditor can conduct an examination of the third party to identify those assets or obligations owed to the judgment debtor so they may be used to satisfy the judgment.

The judgment creditor can also subpoena the judgment debtor's bank statements, checks, deeds of trust, paycheck stubs, and any other document that may identify the judgment debtor's income and assets that may be executed upon to satisfy the judgment.

Once the judgment creditor identifies the assets of the judgment debtor, the

Once the judgment creditor identifies the assets of the judgment debtor, the creditor has a myriad of means by which to enforce the judgment, depending on the nature of the assets.

creditor has a myriad of means by which to enforce the judgment, depending on the nature of the assets. For instance, a creditor can attach a judgment lien against the judgment debtor's real property by obtaining an Abstract of Judgment from the court clerk and recording it with the county recorder's office in each county where the debtor owns or may own real property. Upon the recording of the Abstract of Judgment, a lien attaches to any real property the debtor owns or will own in the county where the Abstract is recorded. If the real property is sold, the judgment will be paid out of the proceeds of the sale in accordance with the priority of the various liens attached to the property. Alternatively, a judgment creditor may choose to foreclose on its judgment lien by means of a sheriff's sale. However, a foreclosure is only feasible if there is sufficient equity in the property to pay off all of the liens senior to the judgment lien, the judgment, and the cost of the foreclosure sale.

In contrast to real property, a judgment does not become a lien on personal property until it attaches. The manner of attachment varies depending on the type of personal property. In most instances, the judgment creditor must first obtain a writ of execution from the court directing the sheriff or marshal to take enforcement actions in the county where the assets are located. Thereafter, the creditor may take the following non-exhaustive enforcement actions depending on the type of personal property involved:

Wage garnishment. If the debtor earns a wage, and is employed by others and not self-employed, the creditor can levy execution on the debtor's wage by obtaining an earnings withholding order to garnish the debtor's wage until the judgment is fully paid. The creditor can collect up to 25% of the amount over the federal minimum wage that the debtor earns, so long as the wage is not exempt under other rules.

Bank levy. The creditor can levy execution on the debtor's checking and savings accounts, and safe deposit boxes to collect on the judgment. A bank levy requires the name (and, in some instances, the branch address) of the bank, as well as the account number of the debtor. This information can be obtained during the judgment debtor's examination discussed above.

Levy of tangible personal property. For tangible personal property such as vehicles or equipment, the judgment creditor can obtain a writ of possession, levy execution on the personal property, and cause them to be sold at sheriff's sale with net proceeds applied towards reduction of the judgment. However, because these types of tangible personal property tend to be either encumbered by senior liens or without significant value, they rarely impart much value to the judgment creditor.

Assignment order. Where a judgment debtor is entitled to receive payments from a third party, *e.g.*, accounts receivable, rents, commissions, royalties, judgments, the judgment creditor can move the court



Bob Benjy is a litigator whose practice emphasizes creditors' rights litigation, defense of lender liability actions and post-judgment collections.



Chun Hsu's practice emphasizes business, creditors' rights and real estate litigation in federal and state courts.

for an assignment order assigning to it the judgment debtor's right to the payments due, or to become due, from the third party.

Charging order. Where a judgment debtor is a partner of a partnership or a member of a limited liability company, the judgment creditor can obtain a charging order from the court to charge the debtor's economic interest in the partnership or limited liability company with the amount of the judgment.

A charging order only gives the judgment creditor the rights of an assignee of the economic interest such as the right to receive partnership or membership distributions to which the judgment debtor would be entitled. A charging order does not entitle the judgment creditor to exercise any voting rights or control over the entity.

Domestication and Registration of Non-California Judgments

Even if a judgment was not rendered originally by a California court, it nevertheless may be enforced in California as a California judgment if the judgment creditor domesticates or registers that foreign judgment in California. Once domesticated or registered, the foreign judgment has the same effect, and may be enforced in the same manner, as a California judgment. The domestication or registration process is different for a state court judgment entered originally by a court in a sister state versus a federal judgment entered originally by a federal court outside of California.

Procedurally, in order to domesticate a sister state judgment in California, the judgment creditor may file an Application for Entry of Judgment ("Application") in the superior court in the county where the judgment debtor resides or in any county if the debtor is a non-resident, with a certified copy of the sister state judgment attached. The Application must state, among other things, the unpaid balance due under the judgment, the amount of accrued interest at the rate allowed by the sister state, and the amount of the filing fee for the Application.

Upon receipt of the Application, the superior court clerk enters the judgment in the same manner as entry of an original judgment of the California court, and the judgment has the same effect as a California judgment. Post-judgment interest be-

The creditor can collect up to 25% of the amount over the federal minimum wage that the debtor earns, so long as the wage is not exempt under other rules.

gins to accrue at the California rate of interest, which is 10% per year, upon entry of judgment,

The domesticated sister state judgment is not immediately enforceable upon entry. Instead, the judgment creditor must serve a Notice of Entry of Judgment on the judgment debtor who will then have 30 days from the date of service to challenge the judgment by filing a motion to vacate. A motion to vacate the judgment can be based on any ground which would constitute a defense to an action in California on the sister state judgment including lack of jurisdiction by the court in the sister state over the parties or the subject matter of the case or a pending appeal of the judgment in the sister state.

However, the judgment debtor cannot challenge the validity of the domesticated judgment by re-litigating the merits of the underlying case. A valid judgment rendered by the sister state court has collateral *estoppels* (issue preclusion) and *res judicata* (claim preclusion) effects in California.

If the judgment debtor has not moved to vacate the domesticated sister state judgment within 30 days from the date of service of the Notice of Entry of Judgment and no stay has been entered, the domesticated judgment "shall have the same effect as an original money judgment of the court

and may be enforced or satisfied in like manner" in California. California Code of Civil Procedure §1710.35.

Registering a judgment entered by a federal court outside of California is simpler than domesticating a sister state judgment. A judgment creditor can register a Non-California federal judgment by filing a certified copy of the judgment with the local district court in California.

Once registered, a non-California federal judgment has "the same effect as a judgment of the district court where registered and may be enforced in like manner." 28 U.S.C. § 1963. Therefore, unlike a domesticated sister state judgment, a registered federal judgment is immediately enforceable and need not be served on the judgment debtor and stayed for 30 days after service.

Since federal district courts apply judgment enforcement laws of the states in which they sit, once registered in California, a federal judgment may have a more favorable statute of limitations for enforcement as compared to the state in which the judgment originated.

For instance, a judgment entered by a federal district court in New Mexico is subject to New Mexico's statute of limitations, which is a maximum of 14 years, with no possibility of renewal. However, so long as said judgment is registered in California before it expires in New Mexico, it adopts the statute of limitations of a California judgment, which is 10 years and is renewable. The 10-year statute of limitations begins to accrue at the time the judgment is registered in California, and not the date of the original entry of judgment. The registered judgment is also renewable pursuant to California law.

Based on the foregoing, a judgment creditor has many means by which to enforce and collect on a money judgment in California. It is imperative for the judgment creditor to take timely actions to examine the judgment debtor to identify assets to attach and take enforcement actions before those assets can be divested or dissipated by the judgment debtor. ■

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