
ALERT

Nevada Developer's Lack of Contact With California Investors Precludes California Court's Exercise of Personal Jurisdiction

On June 10, 2020, in the case of *Farina v. SAVWCL III, LLC*, Docket No. No. B294516, the California Court of Appeal, Second Appellate District, Division Eight, addressed the question whether California courts may exercise personal jurisdiction over a non-California real estate developer who raised money from investors in several states through a hard money broker, but was not aware that a portion of the funds were raised from California investors.

The case involved a Nevada real estate developer and related individuals and entities (collectively, the “Developers”), who used the services of a Nevada-based hard money broker. The broker would raise money from individual investors around the country and pool the money into loans for property developers. The Developers in this case used two (2) loans to purchase property in Nevada for development. The Developers’ loans were funded by over 500 investors, the majority of whom lived in Nevada, about one-fifth of whom lived in other states and about one-tenth of whom lived in California. Each investor was a holder on the promissory notes for the subject loans, and the notes provided that the Developers would make payment to the broker’s Las Vegas address. Each individual lender entered into a loan servicing agreement with the broker, which made the broker the lender’s agent to service each promissory note, to protect each lender’s interest in and enforce the lender’s rights under each note and, if necessary, to manage, refinance and/or sell a property. The investors would provide the loan funds to the broker, who in turn gave the money to the Developers. Loan payments from the Developers to the investors also funneled through the broker.

When the real estate crash occurred and the Developers were unable to make their loan payments, the Developers, through the broker, convinced the investors to relinquish their interests in the promissory notes, deeds of trust and personal guaranties on the loans, and to convert the loans into equity in a new joint venture that would take over the development of the property. The Developers ultimately sold the Nevada property that was purchased with the investors’ loans at a massive loss and distributed the proceeds to the investors for a return of only 17 cents on each dollar the investors lent. The California investors sued the Developers in California, asserting causes of action for fraud, breach of contract and elder abuse, among other things. The Developers moved to quash service for lack of personal jurisdiction.

The court emphasized that the primary concern when assessing case-linked jurisdiction is the burden that such jurisdiction imposes upon an out-of-state defendant. This encompasses not only the practical problems of litigating in a foreign court, but also “the more abstract matter of submitting to the coercive power of a State that may have little legitimate interest in the claims in question”. The court analyzed whether it was proper for California to exercise “case-linked” jurisdiction over the Developers, in which the exercise of personal jurisdiction is predicated on a defendant’s contact with the forum state. Case-linked jurisdiction exists where: (9) the defendant has purposefully availed itself of a forum state’s benefits, (2) the controversy relates to or arises out of the defendant’s contact with the forum and (3) the exercise of jurisdiction comports with fair play and substantial justice.

The issue in this case was whether the Developers had purposely availed themselves of California’s benefits. The court stated that a defendant purposely avails itself of a forum state’s benefits if it intentionally directs its activities at a forum such that, by virtue of the benefits the defendant receives, the defendant should reasonably expect to be haled into the forum state’s courts. The

“purposefully availed” requirement ensures that a defendant is not haled into another state’s courts solely as a result of incidental or attenuated contacts or because of the unilateral activity of another party. The intentions and actions of one party cannot be imputed to other parties.

The court stated that, in order to be sued in California as a result of your business activities, you must intend that your business will benefit from California. In this case, the court found that there was no reason that the Developers should have known or cared where the investors were located. The Developers received the loan funds from the broker, not from the individual investors, and made payments to the broker’s Las Vegas office, not to the individual investors. Because the Developers did not know that a portion of the loan funds came from California and did not intentionally avail themselves of the benefits of doing business with California, the Developers could not be sued in California.

If you have any questions about the jurisdiction of California courts over non-California business entities and other issues that may arise out of multi-state equity raising, please do not hesitate to contact us.



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