2d Civil No. B142310
Consolidated with 2d Civil No. B143705

IN THE COURT OF APPEAL

STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION THREE

SUMMIT INDUSTRIES OF NEVADA, INC., et al.,

Plaintiffs, Cross-Defendants and Respondents,

v.

LOS ANGELES COMMUNITY DEVELOPMENT BANK,

Defendant, Cross-Complainant and Appellant.

Appeal from the Los Angeles County Superior Court
Honorable William J. Birney
Los Angeles Superior Court Case No. VC027696

APPELLANT'S OPENING BRIEF

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INTRODUCTION

The Los Angeles Community Development Bank suffered an $11.7 million judgment in favor of a borrower who was seriously delinquent on a $2.5 million loan, who failed to perform every meaningful covenant of its loan agreement, and whose president and sole shareholder admitted at trial that he had repeatedly lied to the bank.

Every component of the judgment manifests fundamental errors, including these:

- Liability is based on a breach-of-contract theory that the trial court admittedly invented and that is flatly contrary to settled law.
- Even though the sole basis for the judgment is the bank's supposed breach of a contract with its borrower, the judgment also runs in favor of the borrower's sole shareholder, who was not a party to the contract.
- No substantial evidence supports the damages award.
- The judgment includes over $2 million in interest that the trial court awarded in a way and for a purpose that no statute or decision permits.
- The $2.4 million attorney's fee award is based on a lodestar number that is unsupported by a single time record and that is so high that the trial court would have had to believe that plaintiffs' counsel, nearly 30 years in practice, regularly billed over 3,300 hours a year.
- Apparently feeling that this extravagance was insufficient, the trial court enhanced the fee award with a four-times multiplier—virtually unprecedented in California, and unsupported by anything in the record.

These rulings would be troubling even in a case against a large commercial bank. The result is worse here, because the trial court believed its uniquely burdensome theory of liability is particularly suitable for a non-

profit community development lender whose mission is to create jobs in poverty-stricken areas of Los Angeles. The court's paradoxical rationale is that because this kind of lender typically makes much riskier loans than conventional lenders, it has fewer rights.

The judgment should be reversed, with directions to enter judgment for the Los Angeles Community Development Bank.

STATEMENT OF FACTS

A. The Parties.

1. Plaintiffs: Lindsey Austin and his company, Summit Industries of Nevada, Inc.

Lindsey Austin is an experienced and sophisticated businessman. Named Orange County's 1984 "Businessman of the Year" (RT 623) and selected by Newt Gingrich as California's 1998 Republican Businessman of the Year (RT 623), he has been running businesses for over 40 years (RT 620) and has extensive experience working with bankers (RT 681).[1]

During the period relevant to this appeal, Austin was the Chairman, CEO, and sole shareholder of plaintiff Summit Industries of Nevada, Inc.

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[1] We use the following citation conventions in addition to "RT" and "CT": (1) *Exhibits*: In many cases the same exhibit was marked by both sides with different numbers, LACDB using numbers 1-199 and plaintiffs using 201 and up. Citations to the double-marked exhibits include both numbers—e.g., "Ex. 1/208" refers to the document marked as Exhibit 1 by LACDB and as Exhibit 208 by plaintiffs. Many of the exhibits were "Bates" numbered; where it is useful for clarity, we include those numbers (e.g., "Ex. 15/203, Bates 148"). (2) *Post-Trial Proceedings*: These are the subject of consolidated appeal 2d Civ. No. B143705, which has a separate appellate record, cited as "CT2" for the clerk's transcript and "RT2" for the reporter's transcript. (3) *Request for Judicial Notice*: "RJN Ex. __" refers to the exhibits in the concurrently-filed Bates-numbered request.

(RT 618.) Summit manufactured, sold and installed cultured stone counter tops and related kitchen and bathroom items. (Ex. 202, p. 1; RT 635.) Its manufacturing arm, Industrias Sandelos S.A., was a maquiladora plant near Tijuana, Mexico. (Ex. 202, p. 1.) Summit brought its products to a warehouse and distribution facility in Southern California and sold them to home improvement stores and to the construction industry. (*Ibid.*)

2. Defendant: The Los Angeles Community Development Bank.

The Los Angeles Community Development Bank ("LACDB") rose from the ashes of the 1992 civil unrest. It is a nonprofit, public benefit corporation, created with funds borrowed from the federal Department of Housing and Urban Development. (RT 4237; CT 559.) Its mission is to create jobs for residents of a group of impoverished areas of Los Angeles known as the Empowerment Zone ("zone"), a 19-square-mile collection of such communities as South Central Los Angeles, Boyle Heights and Watts. (CT 559, 565.)

LACDB pursues its mission by making loans to businesses that agree to locate in the zone and create employment opportunities there, but cannot obtain credit from traditional lending sources. (RT 4237.) In fact, one of the requirements for a loan from LACDB is the borrower's rejection by conventional lenders. (RT 666-667, 2145.)

B. Summit's Lender Refuses To Extend Summit Any Further Credit, And Introduces It To LACDB.

When Austin first became involved with Summit, the company was "losing money hand over fist." (RT 629.) Austin, as a turnaround specialist, was brought in to "stop the bleeding." (*Ibid.*) The company was

then being financed by a factoring company known as Pine Cobble.[2] (RT 651-652.) Summit assigned Pine Cobble its accounts receivable in return for an immediate payment of a percentage of the amount owing. (*Ibid.*) Summit also had a purchase order line of credit, under which Pine Cobble advanced funds upon receipt of purchase orders so that Summit had the funds with which to satisfy the orders. (RT 662-663.)

This financing was extremely expensive, up to 5% per month. (RT 651-652.) By the time of the LACDB loan, Summit was paying Pine Cobble almost 30% of its gross revenue. (RT 1569-1572, 5257-5258; Ex. 60, Bates 375 [$1.161 million in interest and fees against $3.6 million in gross revenue for the first nine months of 1997]; see Ex. 202, p. 7 ["factoring line is priced at 2.5% for every 15-day period"], Ex. 15/203, Bates 157 [Pine Cobble's interest rates 3-5% per month].)

The events that led up to the LACDB loan began in late 1996. Pine Cobble "needed to cleanup [*sic*] [its] credit facility" (apparently meaning Pine Cobble's own lenders), and this meant that Summit would have to borrow from another lender to pay off its debt to Pine Cobble. (RT 667.) Arman Walker of Pine Cobble said that "we need to get you a lender that can do this. Being a new company and growing as fast, a conventional bank won't be able to handle it." (*Ibid.*)

Don Perry, Pine Cobble's senior vice president, knew of LACDB, and he introduced Austin to Marv West, a LACDB loan officer. (RT 666-667.) Austin told West that he was "willing to open up in the zone." (RT 668.) However, West said that in order for LACDB to consider Summit's loan request, "[w]e had had [*sic*] to have a turn down letter from a bank." (RT 667.)

Summit had not in fact been turned down, but that was easy to fix. Pine Cobble sent Summit a letter stating that it wanted to end their

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[2] A "factor" is one who accepts accounts receivable as security for short-term loans. (Random House Unabridged Dictionary (2d ed. 1993), p. 691, col. 1.)

relationship—even though at the time its actual plan was to buy an interest in Summit. (Ex. 201; RT 678, 709.)[3]

Pine Cobble's Perry furthered the process by preparing financial statements and a "business overview and analysis" of Summit for LACDB. (RT 674-678; Ex. 202.) The business overview said that Summit needed $2.5 million to replace the existing accounts receivable factoring line (i.e., Pine Cobble) and to finance the expansion of the company's warehousing and distribution capability. (Ex. 202, p. 7.) Specifically, "the Company intends to open a shipping and staging hub in Southern California" that would generate 57 jobs. (Ex. 202, pp. 9-10.)

C. LACDB Agrees To Lend Summit $2.5 Million.

In May 1997, West used the information provided by Summit (but prepared by Perry) in an internal "Executive Summary" of the proposed loan application. (Ex. 15/203.) According to the summary, the proceeds would be used to pay off Summit's debt to Pine Cobble, and Pine Cobble would continue to provide short-term accounts receivable financing. (Ex. 15/203, Bates 157.) The summary also stated that Summit's net worth was $7.1 million. (Ex. 15/203, Bates 165.)

In June, LACDB sent Austin a proposed commitment letter for a $2.5 million loan. The letter stated that the proceeds were to be used to "repay short term indebtedness in the aggregate principal amount of $2,500,000 owed to Pine Cobble Partners" and that "sustainable jobs will be created for residents of the [zone]." (Ex. 16, Bates 140.) In addition,

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[3] The trial judge sensed this ambivalence in the letter, calling it "curious" and noting that even as he congratulated Summit on its success, the letter's author also said that "he doesn't want to deal with you anymore. It's like he's shining you on there. . . . I suspect there is another reason why he doesn't want to deal with Summit anymore." (RT 665-666.) Austin volunteered the reason: "Marv West had asked for a letter of turn down." (*Ibid.*) There is no evidence that anyone told LACDB that the turndown letter it required was collusive.

LACDB required "[v]erification of clear title on the Company's assets being utilized as collateral." (*Id.*, Bates 141.)

Austin replied a week later that these conditions were "no problem." Title verification was "no problem as Pine Cobble is the only UCC-1 issued and outstanding." (Ex. 17; RT 698-699.) Job creation was also "no problem, we are planning on hiring over 35 people this year." (Ex. 17.) The same with financial information—"all numbers [are] no problem, we will be happy to supply this information to you on a timely basis." (*Ibid.*)

D. The Deal Keeps Changing.

In the transmittal letter that accompanied Summit's signed copy of the commitment letter, Austin and Pine Cobble President George McDaniel jointly asked LACDB to fund the entire $2.5 million directly to Pine Cobble, which would then pay $500,000 to Summit. (Ex. 19.) (Not revealed in the letter—or at any other time before trial, as far as the evidence shows—was a plan for Pine Cobble to also "rebate" additional funds between $800,000 and $1,200,000 in connection with its purchase of an interest in Summit. (RT 708-709.))

Then problems arose. LACDB discovered unresolved tax liens against Austin; Summit and Pine Cobble began disputing the amount of Summit's debt; and Pine Cobble started slowing its funding. (RT 672-673, 711-713, 1642-1643, 2304, 2306.) At one point Austin backed out of the loan, telling LACDB that Pine Cobble was not funding Summit and did not appear able to act as its accounts receivable lender. (Ex. 20/206; RT 710-712, 1575-1576.) Disaster was imminent. By late August, Austin told LACDB that Summit was on credit hold with key vendors, had a shortage of cash flow, and "will not be able to meet it's [*sic*] current obligations under it's [*sic*] current circumstances." (Ex. 20/206.) But LACDB helped keep the deal together by agreeing to subordinate its security interest to Pine Cobble or another factor. (RT 717-719.) By September 2 the deal was back in place, but now Austin was proposing that Pine Cobble receive $1,750,000 and Summit $750,000. (Ex. 22; RT 1649-1650.)

The uncertainties created by Austin's unresolved tax liens required further changes in the disbursement structure. (RT 4246; see RT 1650 [disbursement instructions were changing "daily"].) Ultimately, Summit agreed to provide LACDB with security against the tax liens by posting a letter of credit, to be issued by Founders National Bank; Founders, in turn, was to hold $456,000 of the loan proceeds as its security. (Exs. 24, 25, 27; RT 729, 2415, 2427, 4246.)

E. The September 5 Loan Agreement (Ex. 208).

LACDB presented Austin with a loan agreement and related documents. (RT 723-724.) Austin testified that he read some of the conditions of the agreement and found it "pretty much boilerplate." (RT 707.) He willingly signed the loan agreement, and did not claim that he was coerced or rushed into signing it. (RT 726, 1578, 1594-1595.)

The loan agreement provide for a $2.5 million loan. (Ex. 1/208, § 1.33.) The loan proceeds were to be used to "fully repay the Pine Cobble Loan," and LACDB was required to "disburse the proceeds of the Loan directly to Pine Cobble at the closing." (*Id.*, § 2.7.) Following are the principal terms involved in this appeal (section references are to Ex. 1/208):

LACDB's security interest in Summit's assets:

- As a condition to closing, Summit was to provide proof that "any and all Security Interests in the Collateral have been released" with the exception of Pine Cobble. (§ 3.5.)
- Summit represented that except as otherwise disclosed, it "has good title to the Assets free and clear of all Security Interests . . . ." (§ 4.5.)

Summit's obligation to conduct business in the zone:

- As a condition of closing, Summit was to have "leased, purchased, or otherwise procured the use of a warehouse in the Empowerment Zone, which, when operational, shall be used as Borrower's principal warehouse in Southern

California" (§ 3.11), and it represented that its main office was in the zone (§ 4.12).[4]

- Summit was to "create a minimum of 71 new full time jobs . . . . A minimum of 36 of these new positions shall be made available to residents of the Empowerment Zone. Such jobs shall be filled no later than the second anniversary of the disbursement of the loan proceeds . . . ." (§ 3.16.)
- "At all times until the outstanding balance of the Indebtedness has been repaid in full, Borrower's principal Southern California warehouse shall be the warehouse located in the Empowerment Zone . . . ." (§ 5.15.)

Summit's financial condition and reporting obligations:

- Summit represented that its financial statements "truly and completely disclose[d its] financial condition" (§ 4.3), and agreed that LACDB was "entitled to rely upon [Summit's] representations and warranties." (§ 4.17.)
- Summit was to "[m]aintain its books and records in accordance with generally accepted accounting principles" (§ 5.2), submit quarterly and annual balance sheets and income statements certified by a CPA (§§ 5.3.1, 5.3.3), and submit its California Employment Development Department Report of Wages on a quarterly basis (§ 5.3.6).

Enforceability of the loan agreement as written:

- "[N]o alteration of or amendment to this Agreement shall be effective unless given in writing and signed by the party . . . sought to be . . . bound . . . ." (§11.1.)

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[4] It is undisputed that LACDB knew these conditions had not been fulfilled when the loan closed; the parties disputed when and how the conditions should later have been fulfilled.

- Any claimed waiver had to be in writing, and no failure to exercise a right could operate as a waiver of that or any other right. (§ 11.14.)

The loan agreement also delineated various events of default allowing LACDB to accelerate. These included not only payment delinquencies but also the existence of "any event or condition which Lender in good faith believes impairs, or is substantially likely to impair, the prospect of payment or performance . . . ." (§ 9.13.) For payment delinquencies, Summit had no right to cure and was not entitled to any notice of default. (§§ 9.14, 10.)

F. With Summit On The Brink Of Collapse, The Loan Closes.

On September 9, 1997, Austin wrote to Pine Cobble that "[w]e will be out of business this week if we are not funded today." (Ex. 29.)

But the loan did fund. In accordance with instructions Austin signed, LACDB disbursed the $2.5 million loan proceeds as follows:

- $1,279,360 to Pine Cobble;
- $470,640 to Founders for the letter of credit;
- $711,500 to Summit; and
- $38,500 to LACDB for fees and expenses. (Ex. 209; RT 728-730.)

This disbursement left a gap that Summit has never explained. No sooner had the loan funded than Pine Cobble began claiming that Summit owed it over $2,000,000, not the $1,279,360 it received when the loan funded. Its position was that even after the funding, "there is still an outstanding principal balance due which is at least $780,000." (Ex. 30; see Ex. 23.) This claim was consistent with the proposed structure of the loan dating back at least as far as LACDB's June 13 commitment letter. (Ex. 16.) Austin himself stated in a pretrial declaration that $1.8 million of the loan was "going to pay the existing co-lender Pine Cobble Funding

Group." (Ex. 146, Bates 2426, ¶ 5.) But at trial, Austin testified that $1,279,000 "was to pay [Pine Cobble] in full" (RT 729) and that he "[didn't] know why" his pretrial declaration said otherwise (RT 5855).

G. Pine Cobble's Fraud.

About a week later, LACDB's West called Austin "in a panic." (RT 735.) He had learned that instead of holding a first lien against Summit's receivables, LACDB was junior to an entity called Capital Funding, to which Pine Cobble had conveyed its interest in Summit's receivables before the LACDB loan funded. (RT 737-738, 757.) In other words, Pine Cobble had conveyed the same security interest twice—first to Capital, and then to LACDB. (RT 757.)

At the same time, Austin discovered that Summit's customers were receiving calls from multiple entities demanding payment on the same invoices. (RT 742-743.) He testified that orders to Summit then started to decline. (RT 743.)

LACDB was in daily contact with Austin trying to resolve the problem. (RT 758-759.) But "Pine Cobble's attorney was being vicious" and Capital was "holding their [*sic*] ground saying we bought it in good faith, not our problem." (RT 759.) Summit faced the prospect of prolonged litigation that "could have been gone on forever [*sic*]." (RT 767.)

H. The Parties Settle Their Dispute And Amend The Loan Agreement.

In November, the parties settled. (Ex. 44/214.) Summit "agree[d] to make certain payments to CAPITAL from loan proceeds including, but not limited to, the sum of $470,640" in return for the release of Capital's security interest, and Summit "expressly authorize[d] [LACDB] to pay $470,640 in loan proceeds to CAPITAL." (*Id.*, pp. 3, 14.) LACDB, in turn, "agreed, at the direction of SUMMIT, to disburse to CAPITAL the sum of $470,640 from loan proceeds" in return for the assignment of the

receivables. (*Id.*, pp. 3-4.)[5] Summit also granted LACDB a security interest in its existing and future accounts receivable. (*Id.*, p. 4.)

The settlement required an amendment of the loan agreement, which was embodied in the "First Amendment To Business Loan Agreement." (Ex. 2 ["Amendment"].) Under the Amendment, Summit ratified the previous disbursement of the loan proceeds, and then amended the previous disbursement to conform to the settlement. (Ex. 2, Recital G.)

Austin claimed that although the settlement was explained to him over the telephone, all he ever saw was the signature page he signed. (RT 755-767, 1653-1655; see Exs. 41, 43 [complete copies of draft agreements faxed to Austin]; RT 1658-1662 [fax transmission confirmations correctly reflect Austin's office and home telephone numbers].) He said that he went along with the settlement because he "didn't have any choice." (RT 767, 1654.) However, there is no evidence that he objected to the settlement or made any claim that LACDB was doing anything inappropriate. To the contrary—the day before signing the Amendment, Austin wrote LACDB that "all in all, business and opportunities for Summit Industries are looking better and better every day, and all of this is due to the dedication of the staff of the Los Angeles Community Development Bank." (Ex. 45.)

I. Summit's Delinquencies Begin.

1. Summit becomes delinquent on its loan payments, but lies to LACDB about its financial condition.

Almost immediately, Summit became delinquent. It made its first three $43,584 payments (RT 4304-4305), but it was a month late on its January payment (Ex. 51; RT 2354), the late check initially bounced (*ibid.*), and it failed to make the February, March and April payments (RT 1847).

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[5] By this time Founders had returned the funds intended for the letter of credit (RT 4255), and LACDB then held them "as funds conditionally available to [Summit]" (Ex. 2, p. 1).

Austin testified that the cause was a slowdown starting mid-January 1998 and a serious cash squeeze in February and March (RT 920), which stemmed from Pine Cobble's fraud—customers reduced their orders because multiple parties were claiming the right to collect on Summit's accounts. (RT 739, 743, 769, 1532-1533,1667-1668, 1671-1672.)

That's worlds apart from what he was telling LACDB at the time of the events, when he admittedly painted an entirely false picture of Summit's success. In a November 1997 letter, for example, he said that Summit's sales and profits for October 1997 were 16% higher than the previous year, and that "all in all business opportunities for Summit Industries are looking better and better every day." (Ex. 45; RT 1534-1536.) Yet at trial, Austin admitted that these statements to LACDB were "false" and that he was just "rah rahing the bank." (RT 1535.) In fact, "there was a lot of letters sent to the bank doing rah-rah." (RT 1537.)

Similarly, in an April 1998 letter, Austin told LACDB that Summit was "still maintaining Coastal Wood [Products] delivery at 12,000 units per month." (Ex. 61/221.) But at trial, he confessed that the letter was false and that he was "hyping the bank every way I can." (RT 1549.) The truth, as Austin admitted at trial, was that new orders "were nonexistent" (RT 1540) and that Coastal Wood had essentially ceased doing business with Summit after August 1997 (RT 1546-1548).

Even though its sales were supposedly plummeting, Summit's financial statements showed that it spent over $800,000 on equipment. (Ex. 60; RT 1600-1604.) Austin claimed that the transactions were actually leases that did not require a "cash outlay" and that "[y]ou'll find offsets in other parts of the balance sheet" (RT 1604), but in fact there were no such entries (see RT 5264-5273).

2. Summit fails to move into the zone.

LACDB knew that Summit was not actually operating in the zone when the loan closed, despite what the loan agreement said. (Ex. 1/208, § 3.11; RT 2184, 2190.) But Austin told LACDB that he had found a property in the zone on Bay Street (RT 2177-2178, 2349-2350), and the loan agreement showed Bay Street as Summit's address (Ex. 1/208, § 4.12; RT 907). It turned out, however, that the site had earthquake problems that would have created too great a delay (RT 908-910), and before the loan funded Austin told the bank he was looking elsewhere (RT 2178-2179).

On September 2, 1997 Austin wrote to LACDB to say he had "struck a deal" on a property on 50th Street, "in the heart of your redevelopment district." (Ex. 22.) But then he told LACDB that the deal fell through because of asbestos problems and the property's unsuitability for loading docks. (RT 2188.) Austin continued to look for a suitable space City of Los Angeles assistance, but six months after the loan funded there were still no live prospects. (RT 916-918.)

J. LACDB Warns Summit About Its Delinquencies.

During the first quarter of 1998, Austin asked West for a six-month forbearance on loan principal payments and for additional assistance in locating Summit's operations in the zone. (RT 920-921.) West responded that consideration of a forbearance was not in the offing so long as Summit was located outside the zone—"getting into this zone was absolutely the number one priority." (RT 922-923.) He also said that "There would not be a monetary problem once I got into the zone." (RT 923.) However, Austin admitted that "he didn't say it [money] was not important" (RT 927), and there was no evidence that West had authority to grant any forbearance (see RT 2466 [West states he did not have that authority]).

On February 24, West wrote to Austin to warn him of Summit's default status. (Ex. 51.) His letter noted that Summit was in monetary default, still had not located a facility in the zone as required by the loan

agreement, and had failed to submit financial and employment information as it had committed to do. (*Ibid.*) West expressed his frustration with Summit's lack of progress:

> "Lin, you know that I am one of your biggest supporters, but I find it extremely difficult to discuss Summit's successes on the one hand and failure to comply with the terms of its loan agreement on the other with this Bank's management. What is more confusing is trying to explain how I am being told that your business is growing with orders coming in all the time with the fact that the Company does not pay or perform as agreed." (*Ibid.*)

Thereafter, West reminded Austin of Summit's noncompliance issues "almost in every conversation." (RT 2359.)

On March 19, LACDB sent a formal notice of default to Summit's main office in Santa Fe Springs. (Ex. 6/217.) The notice went by registered mail and Summit's receptionist signed for it. (RT 1679-1680; Ex. 6/217.) However, Austin testified that he never knew about the notice—the receptionist "received hundreds of letters a day," he was in Summit's Mexico plant at the time, and his employees never told him about it. (RT 1679-1680; 1952-1953.) The notice listed three defaults: (1) default on indebtedness, (2) failure to locate a warehouse in the zone, and (3) failure to submit required financial information concerning Summit's condition. (Ex. 6/217.) Under the loan agreement, Summit had 30 days to cure non-monetary defaults. (Ex. 1/208, § 9.14; Ex. 6/217.) LACDB had no obligation to give notice of monetary defaults, and Summit had no right to cure. (*Ibid.*)

During this period, Vincent Pitts in LACDB's Loan Administration Department, which was responsible for handling troubled loans, succeeded West as the person responsible for the Summit loan. (RT 4937-4939.) Austin didn't get along with Pitts, who insisted that Summit get into compliance. (RT 928-931.) One result was that "clandestinely I [Austin] talked to Mr. West at his residence numerous occasions." (RT 931.)

K. LACDB And Summit Attempt To Resolve The Defaults.

About two weeks after LACDB issued the Notice of Default, it agreed to meet with Summit to discuss how Summit's defaults might be resolved. (RT 934, 3308.) Austin testified that he wanted to meet because Pitts was not returning his phone calls and faxes. (RT 934, 941.)

Austin also wrote to West—though he knew West was no longer responsible for the loan (RT 941; but see RT 947)—to ask that Summit be excused from making monthly payments until June because of cash flow problems, which Austin attributed to the cost of a recent expansion in Summit's product lines. (Ex. 54/220; RT 929.) He did not mention any decline in orders. (Ex. 54/220.) LACDB told Austin that a forbearance "could not be considered without updated financial information." (Ex. 56, ¶ 2, Ex. 59, ¶ 2; see RT 2379-2380 [Ex. 59 is a revision of Ex. 56].) As of April 20, Summit had not provided this information. (Ex. 58.)

On April 30, Summit had not made up its delinquent payments, and another payment was due—a total of almost $175,000. (See RT 1848-1849.) It submitted four checks totaling $43,584, with instructions to deposit one a week. (Ex. 219 [checks no. 31112-31115].) But that still left it $129,000 behind. (Ex. 224 [$129,000 needed by end of June].)

L. The May 27 Meeting.

On May 27, 1998, Austin met again with a group of LACDB officials, including West, Pitts, and others. (RT 947-948.)

The participants discussed Austin's plans to obtain accounts receivable financing. (RT 958; Exs. 63/223, 225.) LACDB was willing to subordinate its senior lien on Summit's receivables, so long as the proceeds went to cure Summit's delinquency. (RT 958.) Austin agreed to obtain an accounts receivable lender by the middle of June, saying it would be "extremely easy" to line one up. (RT 958, 960.)

According to LACDB's summary of the meeting (Ex. 63/223), Austin agreed to bring the loan current by June 30, but in his own letter

following the meeting he was pessimistic—"I do not believe this will happen." (Ex. 225.) Austin also promised to provide by May 29 the California Employment Development Department (EDD) reports that Summit was required to submit to LACDB each quarter. (Ex. 63/223.) These reports were critical for verifying that Summit was making progress on hiring persons in the zone, LACDB's *raison d'être*. (RT 3030, 3656.) Finally, Austin agreed to continue his search for property in the zone. (Exs. 63/223, 225.)

M. Events Following The May 27 Meeting.

One of the disputes concerning post-May 27 events is whether LACDB did what Austin said it agreed to do with respect to subordinating its security interest to an accounts receivable lender.

According to Austin, the terms on which the accounts receivable lender would lend would depend on the nature of LACDB's subordination agreement. He testified that the lender would have to know exactly what LACDB was willing to subordinate to, as well as "what the subordination agreement language is, if they are in fact secured, and they won't even quote you until then." (RT 959.)

But LACDB's witnesses testified that LACDB was never prepared to provide an advance blanket subordination agreement, which is what Austin was apparently describing. (E.g., Ex. 226.) One experienced LACDB officer, Gordon LeJeune (see RT 3603-3604), gave undisputed testimony that in 24 years of banking he had never seen a blanket agreement to subordinate—it would be "like giving a blank check" and thus grounds for a regulatory penalty (RT 4303). West explained that when LACDB was considering subordination to another lender, it was up to the borrower to choose the lender, negotiate the terms, and then present a specific proposal to LACDB. (RT 2320-2321, 2325.) LACDB would then evaluate whether, and on what terms, it would be prepared to subordinate, taking into account the financial condition of the borrower and the cash-

flow consequences of the new obligation. (*Ibid.*) Only then could LACDB draft a proposed subordination agreement. (RT 2325.)

Austin testified that he identified three lenders willing to provide accounts receivable financing. (RT 968.) But there was no evidence that he ever sent anything to LACDB besides a letter one that of the companies, National Factoring Services, sent him in response to an inquiry. (Ex. 66.) This letter described National Factoring's services and was accompanied by a blank application form. (*Ibid.*; RT 4300-4301.) LACDB couldn't do anything with a blank application form; it needed a commitment letter and term sheet to evaluate the transaction before determining the terms of any subordination. (RT 4301, 4944-4945.) There was no evidence that the National Factoring letter constituted any kind of commitment letter; LACDB's Stephen Pastor said it was only "an expression of interest." (RT 3117.) There was also no evidence that Summit ever completed National Factoring's application or that it provided LACDB with a commitment letter or term sheet from National Factoring or any other lender. And no lender ever contacted LACDB. (RT 4944-4947.)

Austin evidently expected LACDB to send him a subordination agreement before he identified a lender. He testified that he repeatedly called and wrote Pitts, who Austin believed was responsible for preparing such an agreement, about where it was. (RT 968, 971-972, 974-977; Exs. 224-226.) Pitts never responded. (RT 977-978.)

In any event, Summit never obtained accounts receivable financing.

N. The June 29 Meeting.

Summit kept falling further behind. In June it paid only $20,000. (RT 982.) And it had made no progress on its obligation to locate a warehouse in the zone.

On June 29, 1998, Austin met with Pastor, LACDB's Chief Credit Officer. Pastor told Austin that LACDB would default Summit if it had not moved into zone by July 11; in Austin's words, "that was [Pastor's] drop-

dead date." (Ex. 228; RT 1202-1203.) Austin "promised him I would get it done, no matter what it took" (RT 1833), even though he had no building in mind at the time (RT 1203). Pastor gave Austin a list of issues that had to be resolved, as well as a timetable for resolving them. (RT 1205.) They also discussed Summit's cash flow problems. (RT 1207-1208.) According to Austin, Pastor said that if Summit got into the zone, "we'll work with the money issue." (RT 1209.)

O. Events Following The June 29 Meeting.

1. Summit's checks bounce.

On July 1, when another $43,000 payment came due, Austin sent LACDB 11 checks totaling $33,000, asking it to deposit one check each day until the middle of the month, when he promised to send another batch of checks. (Exs. 229, 219 [checks no. 51949 et seq.]; RT 984.)

At least three of these checks bounced. (RT 985, 1212; Ex. 165.) Austin testified that he believed they bounced because LACDB deposited them before the dates he requested. (RT 985.) But he also said that they bounced because he told LACDB to "slow down on the deposits a little bit, because I had to draw out a large sum to get into the zone." (RT 1212.)

The promised second set of checks never appeared. On July 15, Austin promised to send $30,000 the next day. (Ex. 232.) He testified that he could not recall whether he sent the checks (RT 1230-1231, 1852); that he "probably" sent them (RT 1234); and that he did send them (RT 1233-1235, 1855). But no such checks surfaced at trial, and Austin could not account for their absence. (See RT 1851-1859.)

2. Summit finally leases, but still does not begin using, property in the zone.

Austin also found a property in the zone on Mesnager Street, and he told LACDB he was negotiating a lease there. (RT 1214-1216.) Summit

leased the property on July 7, 1998—ten months after the loan funded—and took possession and made some improvements. (RT 1224, 1220-1222.) It ordered some manufacturing equipment to be used there (RT 1226-1228), and Austin decided to have one of the employees from the Santa Fe Springs facility work part-time there (RT 1222). All told, Summit invested about $65,000 in the new facility by the end of July. (RT 1245.)

Shortly after Summit leased the facility, Pastor and LACDB compliance officer Josie Starling (see RT 3159-3160) visited the site briefly and asked about Austin's plans for operating the facility (RT 1225-1227). At some point during this period, he told them that it would take about six weeks to get his equipment in place, and they did not object. (RT 1228-1229.) On July 30, Starling visited the site again. (RT 1284.) In a memo, she detailed what she saw:

> "Upon arrival, the business was closed. The security roll-up doors were locked and it appeared that the business had not been opened that day. . . . While I was talking to the owner, an employee of Summit Industries arrived, and opened the front office. There were three desks, one computer, and a fax machine in the office. No other employees were on site, and the employee was unable to open the warehouse. He also stated that we should call before we visit so that someone would be there to let us in." (Ex. 72/243.)

3. The dispute over hiring zone residents.

The loan agreement required Summit to create, "no later than the second anniversary of the disbursement of the loan proceeds," at least 71 new full-time jobs, a minimum of 36 to be available to zone residents. (Ex. 1/208, § 3.16.) There is no evidence that Summit ever employed any zone residents within the zone. But, "just trying to be accommodating," Summit did hire and provide transportation for "three or four" zone residents to work in its 18-employee Santa Fe Springs facility. (RT 967, 1308, 1319.)

Toward the end of July 1998, Starling complained to Austin that he hadn't created any jobs in the zone—"you had 18 [employees], you still have 18, you haven't hired anybody." (RT 1250; see RT 1308 [Austin acknowledges that the Santa Fe Springs facility always had 18 employees].) Austin's position was that he had, in fact, hired several persons, and that it was "not practical" to hire in the zone without having a building there. (RT 1319.)

Pastor called Austin, "absolutely outraged"; "[w]e argued extensively about this employment situation." (RT 1249.) Austin testified that he told Pastor, "I don't have to hire anybody. I don't have to hire anybody until the last day of the second year." (RT 1251.) When Starling got on the phone, Austin repeated his view: "I don't have to hire anybody, according to my loan document, for two years." (*Ibid.*) Pastor told Austin that he had five days to hire people in the zone and be operating at the Mesnager facility. (RT 1251.)

There was no "rah-rah" or "hype" in Austin's combative response:

> "[I]t's time we stopped screwing with this company. Either we work together to solve the problems at hand or we tank the company and ALL of us take or [*sic*] losses and prepare for an unprecedented legal battle. . . ." (Ex. 69/238.)

P. LACDB Accelerates The Loan; Austin Threatens Political Retribution.

By this time, Summit was in extremis. It was "loosing [*sic*] over $40,000 per week in cash flow" (Ex. 69/238), and its internal financial statements showed that its cash position had deteriorated from positive $345,000 as of September 1997 to negative $46,533 by March 1998 (RT 4327; Ex. 60, Bates 373, 364.) Beyond its substantial monetary default, there could be no possible doubt that Summit was in a condition that "impair[ed], or [was] substantially likely to impair, the prospect of payment or performance." (Ex. 1/208, § 9.13.)

Austin acknowledged at trial that Summit was never current on its loan (RT 1851), that LACDB never explicitly agreed to any kind of forbearance (RT 1683-1688, 1826-1827), and that orally all it did was tell him to "[s]how payments in good faith, but get into the zone" (RT 1686). He also conceded that there was never a written agreement altering the terms of the loan agreement, as amended. (RT 1321, 1687.)

On August 5, Pastor issued a Notice of Acceleration. (Ex. 7/239; RT 1262-1263, 3057.) The primary basis for the decision to accelerate was Summit's default in payment. (RT 3057, 3059, 3659.) Also mentioned were Summit's failure to provide EDD forms, its failure to meaningfully operate out of a facility in the zone, and its lack of cash flow, although these were not the primary reason for LACDB's decision. (RT 3030, 3059, 3061, 3096, 3120.) Austin acknowledged at trial that Summit had no right to cure monetary defaults. (RT 1955-1956.)

Almost all of Summit's assets were located in Mexico. (RT 1272-1273.) The acceleration triggered a Mexican-law requirement that Summit notify Mexican authorities that it was insolvent; the notification gave them the right, which they exercised, to seize Summit's assets to secure payment of payroll and any other debts. (RT 1268, 1271.)

In strongly worded letters to Pastor, Austin tried to intimidate LACDB. Once again, there was no "rah-rah" or "hype":

> "We owe some back monthly payments, SO what!!! Our paperwork is not to the banks [*sic*] liking as of yet, again SO what??" (Ex. 71/241.)

Austin also threatened political retribution:

> "If you think this is not going to be a hotbed of political activity, your [*sic*] wrong. I was named 'Republican Businessman of the Year' for 1997. Boy is this going to be interesting, after my name came out in the Wall Street Journal, as the Businessman of the Year. This will make for interesting reading, I can see it now, LACDB closing Businessman of the Years [*sic*] business due to

noncompliance. I am also the current sitting 'Chief' of the Republican tax reform committee of Southern California. I even have my very own little gavel given to me personally by Newt Gingrich. . . . [A] lot of people will hear of this ordeal and hear my side of the story." (Ex. 71/241.)

Q. LACDB Obtains The Appointment Of A Receiver.

In September 1998, on LACDB's application, the trial court (Hon. Thomas I. McKnew) appointed David Pasternak as receiver. (CT 250.) The order of appointment granted Pasternak the authority to "take possession, custody and control of all [Summit's] operations." (CT 251.) Although Pasternak was appointed for the benefit of LACDB, he did not consider himself LACDB's agent. (RT 4816-4817.) Pasternak initially considered operating Summit as a going concern (RT 1939-1940, 4823), but he soon learned from Austin that it had been shut down (RT 4825). Austin declined to operate Summit jointly with Pasternak. (RT 4833.)

The receivership was difficult. Virtually all of Summit's assets were in Mexico, and obtaining authority over them took time. (RT 1272-1273, 1963.) In addition, upon LACDB's showing that Austin started to operate Summit's business under a new name, Shasta, the court added this entity to the receivership. (CT 328-358.) (See generally Notice of Motion and Motion for Order Approving Receiver's Final Report, etc., RJN Ex. 1, Bates 3-28.)

More fundamentally, according to the contempt proceeding initiated against Austin (CT 503-528), Austin was not cooperating in handing over the assets and files of Summit and was transferring assets to third parties. (See also CT 328-358 [application to expand receivership].) Austin pled no contest to the contempt charge, and judgment was entered against him. (CT 595-597 [also Ex. 90]; RT 1876-1877.) The judgment recited:

> "Lindsey Austin knew of the Court's Receivership Order and its effect thereto and willfully failed to comply with the Receivership Order by . . . fail[ing] to turn over all assets of

> Summit and Industrias Sandelos to the Receiver; . . . fail[ing] to disclose to the Receiver Summit's ownership interest in the Industrias Sandelos stock; and . . . transferr[ing] the Industrias Sandelos stock to a third party." (CT 596.)

Ultimately, Summit's assets didn't even cover the costs of receivership administration. The assets located in Summit's building were sold to Austin for $2,500. (RT 2613, 4834; CT 499.) Summit's assets in Mexico never yielded any recovery; they were sold at auction to a third party for $58,000. (RT 1963.) In all, the receivership's recovery was around $15-20,000, at a cost of $100,000 in fees. (RT 4884.)

In September 2000, Pasternak submitted his final account and a motion for its approval. (RJN Ex. 1.) Plaintiffs vigorously opposed the motion, claiming that Pasternak was responsible for substantial losses by Summit. Their accusations covered the entire range of his activities. Among other things, they claimed that "Pasternak's inaction caused Summit to lose assets valued in excess of seven million dollars" (RJN Ex. 11, Bates 330; see *id.*, Bates 333 [quoting trial court's finding about Pasternak's conduct]); that Pasternak was inexperienced in dealing with Mexican businesses (*id.*, Bates 330); that he refused Austin's advice (*id.*, Bates 331); that he and his staff "obviously did not conduct a scintilla of their own research" regarding various issues (*id.*, Bates 334); that he caused the "demise" of Shasta Home Products by failing to operate its business (*id.*, Bates 337), that his "statements prevent[ed] investors from investing in Shasta" (*id.*, Bates 340); and that he failed to supervise Shasta (*id.*, Bates 341). In addition, Summit, Austin and Shasta filed petitions for permission to sue Pasternak, setting the hearing for the same day as the hearing on Pasternak's final account. (RJN Exs. 6-8.)

Pasternak's reply included a point-by-point rebuttal of plaintiffs' claims. He declared that plaintiffs' opposition was "full of misstatements and misleading statements" (RJN Ex. 12, Bates 426) and that many of Austin's descriptions of conversations and other events were false (*id.*, Bates 427, 428, 430).

The trial court granted Pasternak's motion. It approved his final account, exonerated his bonds, and ruled that "[a]ll of [his] actions appear to have been proper and in the best interests of this receivership estate and in compliance with this Court's orders." (RJN Exs. 13, 14.) Pasternak served a notice of ruling on December 7, 2000. (RJN Ex. 15.) The order was appealable (*Aviation Brake Systems, Ltd. v. Voorhis* (1982) 133 Cal.App.3d 230, 233), but plaintiffs did not appeal.

STATEMENT OF THE CASE

A. Overview.

Summit and Austin sued LACDB for breach of contract, negligence, fraud, and interference with business relations. (CT 12-24.) LACDB cross-complained for breach of contract, for default under the security agreement and Austin's personal guaranty, and for other relief. (CT 84-109.) Plaintiffs later amended their complaint to add claims for intentional and negligent interference with prospective economic advantage, slander and RICO violations (CT 260-274), but they later deleted these last two claims (CT 463-476).

After a month-long bench trial, the trial court (Hon. William J. Birney) issued a Memorandum of Intended Decision finding for plaintiffs. (CT 1142.) LACDB requested a statement of decision (CT 1169) and objected to plaintiffs' proposed statement of decision (CT 1210). On June 12, 2000, the trial court filed its Statement of Decision and Judgment holding LACDB liable to both Summit and Austin and dismissing LACDB's cross-claims. (CT 1260, 1264.)

B. Summit's Damages Case.

In closing argument, Summit offered two damages calculations. One yielded $14 million, on the basis of Austin's testimony of Summit's value at the outset of the parties' relationship. (RT 6123; see RT 5859.) The other yielded $7.2 million, on the basis of LACDB's internal summary of Summit's financial statements. (RT 2207-2208, 6124-6125.) Summit also requested interest from August 5, 1998, because "[t]hat's when the damage occurred, that's when the loss—that's when the loss was finalized, when the receiver book [*sic*; took] over the business in August of 1998." (RT 6125.)

C. The Statement Of Decision.

The trial court found liability solely for breach of contract and stated that this finding "renders moot" plaintiffs' other claims. (CT 1266:21.)

The trial court's "Workout mode" theory of liability. The statement of decision mirrors a theme the trial court articulated during the trial: Community development lenders must adhere to a higher standard of care in dealing with borrowers than ordinary commercial banks.[6]

The court acknowledged that LACDB would prevail under settled law governing conventional loans, but concluded that "[t]hese clear concepts urged by the Bank obviously do not effect early resolution here." (CT 1268:17-18.) Instead, the trial court struck out on its own, candidly acknowledging later that ". . . I also know that it appears and maybe it will be shown that I fashioned a whole new remedy that, that didn't maybe exist before." (RT2 9.)

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[6] For example, the court observed that "this [case] is different than the Bank of America making a loan. . . . If it wasn't different, we wouldn't even be here. I mean the lender of loans, the borrower fails to repay, he's done." (RT 4212-4213.) The trial court requested authority as to rules governing a "noncommercial bank." (RT 4209.)

Central to the court's analysis was the special nature of the kind of loans LACDB makes, in which borrowers must be unable to qualify for conventional loans. "This circumstance suggests that these loans are such as may require a particular hands on administration from their initiation." (CT 1268:23-24.) Therefore, instead of looking to the parties' written agreements to define their rights, the court relied on a discussion of "workouts" in LACDB's internal Credit Guidelines. (Ex. 180, "Risk Asset Workouts," quoted at CT 1268-1269.)

The court recognized that no written workout agreement existed, but it nevertheless found that "the parties had realistically entered a Workout mode, though undeclared." (CT 1269:25-26.) Dismissing Summit's payment delinquency as a "[t]echnical default" (CT 1270:24), the court determined that liability turned on the "reasonableness in the circumstances" of LACDB's conduct in the context of this undeclared "Workout situation" (CT 1277:21).

The court ultimately based its breach-of-contract finding on a "Workout mode *which may be considered an adjunct to the written loan contracts* between them and from which certain reasonable obligations follow." (CT 1278:2-4, emphasis added.) It found that "[t]he actions between the parties, shifting, disjointed, and without reasonably aggressive and informed management by the Bank were nonetheless such from which there reasonably derived an implied duty of good faith and fair dealing." (CT 1279:4-8.) Under this standard, the court concluded that the foreclosure was not justified and that LACDB breached the contract.

The court denied LACDB any recovery. (CT 1280:13-15.)

Damages based on Summit's supposed value on the date of the loan. Summit did not survive the receivership, and the trial court held LACDB accountable for its total loss. In so doing, the court concluded that the court-appointed "receiver's action, or more specifically inaction, led to the loss of Summit's assets in Mexico which were valued in excess of $7 million," and it held LACDB responsible for losses that it found the receiver caused. (CT 1279:23-25, 1283-1284, ¶ 6.)

The court measured damages as of the date of the loan agreement. (CT 1279:27-28, 1285:5-7.) Characterizing as "unrebutted" the evidence of Summit's value on that day, the court found it was $7,238,047, and charged LACDB with that amount "plus interest at the legal rate." (CT 1280:1-10.)

Prejudgment interest calculated from the date of the loan. Although in closing argument plaintiffs only asked for prejudgment interest from August 1998 (RT 6125), the trial court awarded interest from the date of the loan agreement, totaling $2,004,536.93 (CT 1261:8-11). Its rationale was that "using legal interest from September 5, 1997, is the most conservative, and fairest means to measure the actual economic loss without getting into complex calculations that would become increasingly difficult and argumentative." (CT 1284:24-27.)

Attorney's fees. Finally, the court found that plaintiffs were entitled to their attorney's fees. (CT 1261:11-13.)

D. Judgment

The trial court entered judgment consistent with the statement of decision. Although the statement of decision explicitly imposes liability solely for breach of contract and states no basis for Austin's having any breach-of-contract claim, the judgment is in favor of both Summit and Austin. (CT 1261.) LACDB objected to plaintiffs' proposed judgment (CT 1157) on this ground (CT 1183).

E. Post-Trial Motions.

LACDB moved for a new trial on numerous grounds. (CT2 38.) In its supporting memorandum, LACDB argued that Summit's financial statements, upon which the award of damages was ultimately based, were internally inconsistent and riddled with egregious errors. (CT2 420-432.) LACDB also challenged the award of prejudgment interest, both because the amount of damages was uncertain and because the trial court improperly

used prejudgment interest as a proxy for lost profits. (CT2 432-434.) The court denied LACDB's motion. (CT2 523.)

Plaintiffs requested attorney's fees. (CT2 5.) Over LACDB's opposition (CT2 50), the court awarded $2,421,000 (CT2 523). Since plaintiffs' counsel's standard hourly rate was $250 (CT2 15), the award represented nearly a four-times multiplier of the charge attributable to the 2,500 hours counsel claimed he worked (CT2 17).

F. Statement Of Appealability.

The trial court filed its judgment on June 12, 2000. (CT 1260.) LACDB filed a timely notice of appeal on June 14, 2000. (CT 1305.) The judgment is appealable as a final judgment under Code of Civil Procedure section 904.1, subdivision (a)(1).

The trial court filed its order awarding attorney's fees on August 4, 2000. (CT2 524.) LACDB filed a timely notice of appeal on August 10, 2000. (CT2 529.) The order is appealable as an order entered after judgment under Code of Civil Procedure section 904.1, subdivision (a)(2).

This Court consolidated the two appeals on April 23, 2001.

STANDARD OF REVIEW

Several different standards of review govern this appeal.

The core of the judgment is the trial court's "Workout mode" standard of contractual behavior. Whether such a standard exists is a question of law and therefore subject to de novo review. (*Stratton v. First Nat. Life Ins. Co.* (1989) 210 Cal.App.3d 1071, 1083.) Also subject to de novo review, in the absence of conflicting extrinsic evidence, are any questions concerning the proper interpretation of the parties' written agreements. (*Parsons v. Bristol Development Co.* (1965) 62 Cal.2d 861, 866; see also *Klingele v. Engelman* (1987) 192 Cal.App.3d 1482, 1485

["The interpretation of a written instrument presents a question of law for this court to determine anew."].)

Once the Court determines the correct standard of contractual behavior, questions as to whether LACDB or Summit breached their obligations and as to the propriety of the damages award are governed by the substantial evidence standard of review.

The award of interest raises two distinct questions. The first is whether interest may be awarded as a substitute for lost profits, which is what the trial court appears to have done; that question is purely legal, and is therefore reviewed de novo. (*Stratton v. First Nat. Life Ins. Co.*, *supra*, 210 Cal.App.3d at p. 1083.) The second is whether, assuming interest is otherwise proper, the award complies with the requirements of Civil Code section 3287 that "damages [be] certain, or capable of being made certain by calculation" and that the right to recovery be "vested in [plaintiffs] upon a particular day." That decision is reviewed for abuse of discretion; the review includes whether award is based on "a 'reasoned judgment' and complies with the '. . . legal principles and policies appropriate to the particular matter at issue.'" (*Bullis v. Security Pac. Nat. Bank* (1978) 21 Cal.3d 801, 815.)

Finally, attorney's fees awards are reviewed for abuse of discretion. (*Ramos v. Countrywide Home Loans, Inc.* (2000) 82 Cal.App.4th 615, 621.) In addition, LACDB's contention that lodestar component is unsupported by the evidence invokes the substantial evidence standard of review.

ARGUMENT

I.

THERE IS NO FACTUAL OR LEGAL BASIS FOR THE TRIAL COURT'S CONCLUSION THAT LACDB BREACHED ITS CONTRACTUAL OBLIGATIONS.

A. Overview.

The first place one normally looks to see if a party breached a contract is the written contract itself. That task is unnecessary here. As we demonstrate in Section I.B., the trial court relied entirely on implied obligations, and refused to identify any express provision of the loan agreement that LACDB supposedly breached. That means the judgment can only be affirmed on the basis of a breach of implied obligations.

We next demonstrate that the trial court's invented "Workout mode" theory of liability is contrary to controlling authority and unsound as a matter of policy. (§ I.C.)

Turning to specific claims of breach, the statement of decision identifies two series of events as to which the trial court found that LACDB breached implied obligations. The first is the initial funding of the loan, particularly the fallout from Pine Cobble's fraud and the Amendment to the loan agreement; the second concerns the parties' dealings after Summit went into default in early 1998, and particularly LACDB's acceleration of the loan. In Sections I.D. and I.E., we demonstrate that there is no basis for liability in either area.

Finally, we demonstrate that the absence of support for the judgment in any one of these areas requires reversal. (§ I.F.)

B. There Is No Evidence, And No Finding By The Trial Court, That LACDB Breached Any Express Provision Of The Loan Documents.

Absent from the statement of decision is any suggestion of any breach of any express obligation of the loan agreement. Just the opposite—the trial court *disclaimed* any such finding. Indeed, one of the most distinctive features of the statement of decision is its avowed disregard for the text of the loan agreement.

The statement of decision acknowledges that it "cannot be disputed" that ordinarily a payment default entitles a lender to declare a default and accelerate a loan. (CT 1268:11-14.) But, the statement adds, "[t]hese clear concepts urged by the Bank obviously do not effect early resolution here." (CT 1268:17-18.) It then goes on to posit what it calls "a Workout mode" (e.g., CT 1278-1279) as the basis for all its findings of breach.

Confirmation that the trial court did not and could not find a breach of any express contractual obligation appears in the portion of the statement of decision that responds to specific questions on that subject in LACDB's request for a statement of decision. (CT 1171-1172.) While stating that "[t]he Bank breached its contractual obligations" (CT 1281:25), the statement of decision does not identify a single breached clause, a point emphasized in LACDB's objections to the proposed statement of decision (CT 1222-1224), which became the final statement of decision (see CT 1264; see CT 1287). LACDB has no obligation to show error in findings the trial court refused to make.

Under Code of Civil Procedure 634, the Court cannot fill in the blanks through the usual presumption that the trial court made all factual

findings necessary to support the judgment.[7] It must take the trial court at its word: LACDB did not breach any express contractual obligations.

C. The Trial Court Departed From Settled Law In Imposing A Heightened And Unprecedented Standard Of Liability On LACDB.

The trial court was candid about what it was doing: "[T]here was a wrong done to the plaintiff here, and I tried to fashion a remedy for that wrong." (RT2 16.) Forsaking both the language of the parties' agreement and decisional authority—it doesn't cite a single case—the statement of decision relies instead on LACDB's *internal* "Risk Asset Workout" guidelines (Ex. 180), and posits a "breach of contractual responsibility arising out of a Workout relationship . . . which may be considered an adjunct to the written loan contracts between them . . . ." (CT 1277:28-1278:4.) Apparently, however, this special relationship only arises with community development lenders, since their borrowers cannot qualify for conventional loans and therefore "the risk element involved is obvious immediately and certainly exceeds what the usual commercial bank encounters." (CT 1268:19-23.)

It has long been settled that a court may not imply an obligation that contradicts express contractual rights or duties. Here, the loan agreement explicitly entitled LACDB to take the actions it took. There was accordingly no room for the implied covenant to operate and no basis for the trial court to invoke it in aid of creating a new form of liability.

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[7] "When a statement of decision does not resolve a controverted issue, or if the statement is ambiguous and the record shows that the omission or ambiguity was brought to the attention of the trial court either prior to entry of judgment or in conjunction with a motion under Section 657 or 663, *it shall not be inferred on appeal or upon a motion under Section 657 or 663 that the trial court decided in favor of the prevailing party as to those facts or on that issue*." (Emphasis added.)

1. The implied covenant of good faith and fair dealing derives from and cannot supersede the express terms of the contract.

The covenant of good faith and fair dealing is not, as the trial court seemed to think, a panacea for everything a trial court may feel is somehow unfair. Rather, "[i]t is universally recognized the scope of conduct prohibited by the covenant of good faith is circumscribed by the purposes and express terms of the contract." (*Carma Developers, Inc. v. Marathon Development California, Inc.* (1992) 2 Cal.4th 342, 373.) Its limited role is "merely to prevent one contracting party from unfairly frustrating the other party's right to receive the *benefits of the agreement actually made*." (*Guz v. Bechtel National Inc.* (2000) 24 Cal.4th 317, 349, emphasis in original.)

The covenant therefore "cannot impose substantive terms and conditions beyond those to which the parties actually agreed" (*Starzynski v. Capital Public Radio, Inc.* (2001) 88 Cal.App.4th 33, 39, citing *Guz v. Bechtel National, Inc.*), and "an implication should not be made when the contrary is indicated in clear and express words" (*Carma Developers, Inc. v. Marathon Development California, Inc.*, *supra*, 2 Cal.4th at p. 374, ellipsis and quotation marks omitted). Thus, "there can be no implied covenant where the subject is completely covered by the contract." (*Pacific Gas & Electric Co. v. Superior Court* (1993) 15 Cal.App.4th 576, 608-609, internal quotation marks omitted.)

Most important for our purposes: As our Supreme Court observed in *Carma*, "We are aware of no reported case in which a court has held the covenant of good faith may be read to prohibit a party from doing that which is expressly permitted by an agreement." (*Carma Developers, Inc. v. Marathon Development California, Inc.*, *supra*, 2 Cal.4th at p. 374.)

The trial court's "Workout mode" contravened these principles by creating obligations that contradicted the contract. It imposed liability for LACDB's exercise of express contractual rights, and it conferred upon Summit vastly more than the single contractual benefit promised by the loan agreement—a $2.5 million loan.

2. California appellate courts have squarely rejected the trial court's "Workout mode" theory.

The trial court's theory seems to be this: A lender's freedom to enforce loan obligations in accordance with their terms ends as soon as the lender tries to help get a delinquent borrower back on track. Then, a de facto "Workout mode" arises, governed by a rule of "reasonableness in the circumstances," with the purpose of "avoid[ing] harm to the borrower." (CT 1277:21-24.) This "adjunct to the written loan contracts" purportedly derives from the implied covenant of good faith and fair dealing, and it effectively imposes a duty of forbearance that supersedes the lender's express contractual rights. (CT 1278-1279.)

Established precedent squarely rejects this view.

Price v. Wells Fargo Bank (1989) 213 Cal.App.3d 465 deserves a detailed discussion because it illustrates just how far the trial court diverged from settled law governing lender/borrower contractual relations. In *Price*, the plaintiffs operated a cattle operation. Like Summit here, the *Price* borrowers' current lender refused to provide additional credit, so they went to Wells Fargo for a loan that they were supposed to use to retire their old debt and for operating expenses. (*Id.* at p. 471.)

Wells Fargo officers orally assured the borrowers that it would "redo" the notes. (*Id.* at p. 472.) But when the loan matured and the borrowers sought restructuring, the bank demanded full payment. It agreed to delay foreclosure if the borrowers made further payments under an agreed schedule, but when the borrowers failed to meet this schedule, the bank began foreclosure proceedings. (*Id.* at pp. 472-473.)

However, the bank agreed to forbear setting a trustee's sale if the borrowers met its demand for a payment and asset-assignment schedule that called for payment in full by June 10, 1985. When the borrowers failed to meet this schedule, the bank scheduled a trustee's sale for July 9. The borrowers ultimately paid the outstanding loan balance by June 28. By that

time, however, they had been forced to sell substantial business assets at fire sale prices. (*Id.* at pp. 470-474.)

The borrowers sued, alleging that the bank had breached the implied covenant of good faith and fair dealing "by taking a 'hard line' in repayment negotiations" and that it had not been justified in noticing a foreclosure sale right after accepting a large partial payment. (*Id.* at p. 479.) As the Court of Appeal framed their position, "[t]he necessary implication of [the borrowers'] argument is that the bank owed them a duty of reasonable forbearance in enforcing its creditor's remedies." (*Ibid.*)

The court affirmed summary judgment for the bank. Noting the absence of any authority supporting the borrowers' position, the court flatly rejected it. Rather, the court held, "[c]ontracts are enforceable at law according to their terms," and the implied covenant of good faith and fair dealing "does not impose any affirmative duty of moderation in the enforcement of legal rights." (*Ibid.*)

Price is indistinguishable from the present case. Like Wells Fargo, here LACDB had a contractual right to accelerate the loan upon the borrower's default. Like the *Price* borrowers, Summit went into serious default on its payments. Like Wells Fargo, LACDB tried to work with the borrower instead of immediately foreclosing. Like the *Price* borrowers, Summit could not meet even an adjusted schedule to address the defaults. And finally, LACDB, like Wells Fargo, exercised its enforcement rights despite the borrower's partially successful efforts at compliance, including substantial partial payments. The only thing that distinguishes *Price* from the present case is that the *Price* borrowers ultimately did pay their loan balance; here, Summit never came close.

The trial court's ruling cannot be reconciled with *Price*:

- *Price* held that a lender owed *no* duty of reasonable forbearance in enforcing its contractually-obtained creditors remedies. (213 Cal.App.3d at p. 479.) The trial court here concluded exactly the opposite: that LACDB *had* a contractual duty "to cooperate in good faith with

reasonable workable solutions proposed by the debtor." (CT 1281:16-17.)

- *Price* held that "[c]ontracts are enforceable at law according to their terms." (213 Cal.App.3d at p. 479.) Here, the trial court ignored the written provisions of the loan agreement that gave LACDB the right to accelerate for nonpayment, dismissing Summit's delinquency as a mere "technical default." (CT 1270:24.)
- *Price* held that the implied covenant "does not impose any affirmative duty of moderation in the enforcement of legal rights." (213 Cal.App.3d at p. 479.) The trial court ruled that LACDB's rights were qualified by a duty "to avoid harm to the borrower." (CT 1277:23-24.)

3. Holding community development lenders to a higher standard of care than traditional lenders undermines the goals of community lending.

Recognizing that established precedent required judgment for LACDB (CT 1268:11-16), the trial court singled out community development lenders for the application of a special standard of liability under which a trial court may ignore explicit contract terms negotiated at arm's length in favor of its *post hoc* view of "reasonableness in the circumstances." (CT 1277:21.) And "reasonableness" apparently means that the community development lender must place the borrower's interests ahead not only of its own interests, but also of the goals that community lending is supposed to serve.

It would be hard to exaggerate the negative impact of such a standard on community development lending. Predictability, the cornerstone of contractual relationships, disappears. Unmoored from express contractual rights and duties, in dealing with its borrower the community development lender must guess what a judge or jury might later find "reasonable." The penalty for guessing wrong could be much greater than losing the right to

repayment. It could also include shouldering the blame for the failure of a business that, since it was borrowing from a community development lender, was probably shaky to begin with. And, to top it all off, the lender must pay the borrower's attorney's fees.

It is hard to imagine how any lender could flourish under such a regime, much less a community development lender that every day faces the daunting task of obtaining funds for making loans in areas that the private capital markets have abandoned. At bottom, greater exposure to liability would make community development lending even riskier than it already is—meaning that funding would become more difficult to obtain.

But the real losers wouldn't be the lenders. Rather, the losers would be the true intended beneficiaries of community development loans—those who live and are unable to find work in poverty-stricken areas. Economic empowerment as a remedy for the chronic unemployment and underemployment that plague our cities cannot flourish if this last-resort source of capital dries up because lenders have become subject to a special liability standard.

In crafting special rights for borrowers like Summit, the trial court ignored the fact that serving these borrowers isn't the goal of community development lending. They are supposed to be only *incidental* beneficiaries—a means to an end, a vehicle for the creation of jobs and economic activity. LACDB was not created to promote the success of Lindsey Austin—the "Orange County Businessman of the Year"—or of his company, no matter how troubled it might have been. Rather, its mission is to encourage sophisticated businessmen like Austin to invest in the zone, so that Summit's economic fortune *would benefit zone residents*. (See 24 C.F.R. § 597.2 [empowerment zones created to stimulate job creation for disadvantaged]; Ex. 180, "Loan Administration," § 5.1 [LACDB makes loans to businesses "to create or retain jobs"].)

Summit never came close to serving these goals. Nearly a year after receiving its community development loan, Summit had invested only $65,000 in the zone, had one part-time worker there, and had hired a

handful of workers to work elsewhere. (RT 967, 1222, 1245.) Everything about the borrower's side of this dispute is a paradigm of how community lending is *not* supposed to work.

D. LACDB Did Not Breach Any Express Or Implied Obligation In Connection With The Initial Funding Of The Loan Or The Amendment Of The Loan Agreement.

1. LACDB's pre-delinquency conduct was not and could not have been governed by any "Workout mode."

If even the trial court's "Workout mode" theory had some abstract validity, it could not apply until after Summit became delinquent. That is because, according to the trial court, Summit's February and March 1998 "nonpayments *led to commencement* [*sic*] of what can be reasonably considered a Workout mode between the parties." (CT 1277:4-5, emphasis added; see also CT 1269:23-25 [evidence "strongly suggests that when Summit failed to make the February and March, 1998 monthly payments, the parties had realistically entered a Workout mode"].) Nothing in the statement of decision suggests that the "Workout mode" governed anything concerning the inception of the loan. At most, it says that because of the way in which the Pine Cobble problems were resolved, "additional responsibilities between the parties were created, for which mutual cooperation was required." (CT 1278:9-10.)[8]

Accordingly, any pre-delinquency breach had to arise from LACDB's failure to perform some express provision of the loan agreement

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[8] The statement of decision also says that Capital's actions "required a Workout" between the parties" (CT 1278:10-16), but it does not explain how that situation, which occurred *before* anything occurred that the trial court identified as a Summit default, could give rise the "Workout mode" that the trial court held was *triggered* by a default.

or some act required by the implied covenant of good faith and fair dealing. As we now demonstrate, there was no such breach.

2. LACDB completely performed all of its pre-delinquency obligations.

Although the statement of decision does not identify any particular clauses of the loan agreement that the trial court believed LACDB breached, it does identify supposed pre-delinquency breaches. According to the trial court, LACDB "failed to fully fund the loan and provide the consideration to Summit contemplated by the contract" (CT 1281:26-27) and it "acted in a heavy handed and irresponsible fashion in using money that belonged to Summit to solve the problem caused by the Bank's own negligence in failing to follow its own established guidelines to conduct a UCC search BEFORE funding" (CT 1281:12-15). In addition, "[t]he Bank interfered with Summit's ability to perform by not providing all consideration contemplated by the contract, by causing economic damage to Summit as a result of its errors regarding the UCC filings, [and] by not immediately resolving, with its own assets, the problems that resulted from its error regarding the UCC filing . . . ." (CT 1282:6-11.)

But what obligation, exactly, did LACDB breach? None.

a. No breach in initial funding. LACDB's affirmative obligation at the closing of the loan was simple: Fund the loan as directed by the borrower. There is no possible dispute—LACDB did just that.

As explained in the Statement of Facts (§ D.), the original disbursement plan changed because of the discovery of tax liens and because a dispute arose between Summit and Pine Cobble over the amount that Summit actually owed Pine Cobble. These issues were resolved, for the time, and Summit authorized a multi-party disbursement: $1,279,360 to Pine Cobble; $470,640 to Founders National Bank for a letter of credit in LACDB's favor; $711,500 to Summit; and $38,500 retained by LACDB for

fees and expenses. (Ex. 28; RT 728-730.) This is precisely the disbursement LACDB made. (RT 730-731, 734.)

We are aware of no authority suggesting that a borrower can base any kind of claim on a bank's *adherence* to the borrower's disbursement instructions. (See *Kim v. Sumitomo Bank* (1993) 17 Cal.App.4th 974, 981 ["it is apparent that the [plaintiffs'] objections to the disbursement procedure are before this court because they did not pay attention to what they signed"].)

b. No breach from failure to run UCC search. The trial court concluded that LACDB breached the contract "by causing economic damage to Summit as a result of its [LACDB's] errors regarding the UCC filing" (CT 1282:8-9) and that it was "negligen[t] in failing to follow its own established guidelines to conduct a UCC search BEFORE funding" (CT 1281:14-15). Certainly things would have gone differently if LACDB had discovered Pine Cobble's fraud by re-running the UCC search it had run three weeks earlier on the day it funded the loan. But LACDB owed neither a contractual nor a negligence duty to Summit to perform *any UCC search at all*, much less an additional search on the day of funding. Just the opposite: Under the plain language of the contract, *Summit* was obligated to verify that its assets were free and clear of all liens, and LACDB had the right to rely on the representations Summit made in the loan agreement. (See 1/208, §§ 3.5, 4.12.)

"Nonsensical" is one court's word for the kind of duty the trial court imposed here. (*Nymark v. Heart Fed. Savings & Loan Assn.* (1991) 231 Cal.App.3d 1089, 1100.) In *Nymark*, a borrower alleged that the defendant lender was negligent in appraising his property as part of the approval process for a loan. The court of appeal affirmed summary judgment for the lender, holding that it owed no duty to the borrower to conduct the appraisal properly. Rather, it "performed the appraisal of plaintiff's property in the usual course and scope of its loan processing procedures to protect *defendant's* interest by satisfying it that the property provided adequate security for the loan." (*Id.* at p. 1096, emphasis in original.)

The same is true here. The only reason LACDB needed to conduct a UCC search was to "satisfy[] [itself] that the [receivables] provided adequate security for the loan" (*ibid.*), since their value as security would depend on the priority of LACDB's prospective lien. Neither the loan agreement nor general law required LACDB to perform this search properly. The receivables were Summit's assets, not LACDB's—and, as in *Nymark*, Summit "was in as good a position as, if not better position than, defendant to know the value and condition of the property." (*Id.* at p. 1099.) *Nymark* concluded that imposing liability under facts like these

> "would produce the incongruous result that a lender which conducts an appraisal *for its own benefit* could become responsible for guaranteeing to the borrower the adequacy and soundness of the collateral the borrower has pledged as security for the loan. Such a nonsensical result is not compelled by the law." (*Id.* at p. 1100, emphasis in original.)

*c. **No breach involving the Amendment.*** The statement of decision concludes without explanation that in working to reconfigure the loan in the wake of Pine Cobble's fraud, LACDB "dealt unfairly and took advantage of Summit's necessitous circumstances when it extorted a modification to the contract in November 1997" (CT 1282:22-24) and that LACDB "acted in a heavy handed and irresponsible fashion in using money that belonged to Summit to solve the problem caused by the Bank's negligence" (CT 1281:12-14). No evidence supports this provocative hyperbole, and it defies common sense.

Nothing in the loan agreement required LACDB to take *any action whatever* to help resolve Pine Cobble's fraud. Just the opposite—the fraud gave LACDB the absolute right to declare the loan in default on several grounds, including the failure of Summit's representation of title to its receivables (Ex. 1/208, §§ 4.5, 9.2) and the existence of "any event or condition which Lender in good faith believes impairs, or is substantially likely to impair, the prospect of payment or performance . . . " (*id.*, § 9.13). LACDB would also have been completely within its rights to sit back and

demand that Summit work out the Pine Cobble problem on its own, with its own money, while still keeping current on its loan. And LACDB could have decided to remain in a junior lien position and enforce the remainder of the loan agreement in accordance with its terms.

Yet instead of enforcing its rights, LACDB allowed Summit to use a portion of the loan proceeds to pay Capital, and it gave up its right to a letter of credit as security against tax liens. (See SOF, § I.) At the time, Summit recognized and was grateful for LACDB's efforts, as shown by Austin's letter thanking LACDB for "the dedication of [its] staff." (Ex. 45.)

What, then, is the basis for the trial court's finding that LACDB was "extort[ionate]," "heavy handed and irresponsible"? (CT 1281-1282.) Simple—there is none. There was certainly no extortion in the technical sense—LACDB did not obtain the amendment through the "wrongful use of force or fear." (Pen. Code, § 518.) And if the trial court meant "economic duress," not only did plaintiffs never urge such a claim (see CT 463-476), but they could not have prevailed on it if they had. (E.g., *River Bank America v. Diller* (1995) 38 Cal.App.4th 1400, 1424, 1425 [no duress where bank "unilaterally" changed joint venture to loan with guaranties; partners could have sued to enforce joint venture, but instead "made a business decision to accept the loan and guaranty agreement"].)

d. No breach from LACDB's failure to resolve problems "with its own assets." The trial court's most astonishing finding is that LACDB had to use its own assets to resolve the difficulties Pine Cobble's fraud created. (CT 1282:6-11.) The statement of decision identifies no source for this supposed obligation, other than the erroneous conclusion that LACDB was responsible for creating the problem.

Plaintiffs have never suggested, and the trial court did not find, that either LACDB or anyone else should have anticipated the fraud. And, as we have shown, the loan agreement neither imposed an obligation on LACDB to protect against the fraud nor obligated it to do anything more than stand by its rights under the loan agreement. The statement of decision suggests no authority for the extraordinary proposition that a lender must

use its own money to solve a problem created by a third party's fraud against its borrower, and our research has not revealed any.

Besides, LACDB, not Summit, bore the brunt of the Pine Cobble settlement, at least initially. Although the $470,640 paid to Capital came out of loan proceeds, Summit was not supposed to receive those proceeds at the outset. They were slated to go to Founders to support a letter of credit for LACDB to hold as security against the tax liens. Thus, at least in the short term, the Pine Cobble settlement left Summit exactly where it was supposed to be. In contrast, LACDB gave up the security of a letter of credit, taking instead the receivables that Capital held (see Ex. 2, § 3(ii), p. 3; RT 4264), which ended up yielding only $160,000 (RT 4270).

E. LACDB Did Not Breach Any Express Or Implied Obligation After Summit Became Delinquent.

As noted earlier, the trial court did not identify any express provisions of the loan agreement that it believed LACDB breached; rather, it relied on its "Workout mode" concept to impose liability. We address the failure of that erroneous and unprecedented concept above. (Section I.C., *ante*.) Here, we demonstrate that LACDB did not breach any express contractual provision and did not breach the covenant of good faith and fair dealing as defined by settled law.

1. LACDB had statutory and contractual authority to accelerate the loan, because Summit was in severe default and LACDB had a reasonable basis to believe that its security was impaired.

The trial court found that LACDB breached because "[a]fter declaring a monetary default the Bank accepted payments from the debtor in excess of the declared default and then accelerated without giving further notice and declaring further default." (CT 1281:27-1282:2.) This directly contradicts the written loan agreement, which expressly gave LACDB the

right to do these things. Section 9.14 exempts monetary defaults from the notice-and-cure provisions that apply to other types of default. (See Ex. 1/208, §§ 9.1, 9.14.) The promissory note provides that "upon default, Lender may declare the entire unpaid principal balance on this Note and all accrued unpaid interest immediately due, without notice, and the Borrower will pay that amount." (Ex. 4.) And the loan agreement further provides that no failure to exercise a right operates as a waiver of that or any other right. (Ex. 1/208, § 11.14.)

Besides, LACDB indisputably *did* give notice of Summit's default for failure to pay the monthly payments for the first quarter of 1998 (Ex. 6/217), and Summit never became current—it just fell further behind. LACDB was therefore entirely justified in accelerating the loan for failure to make the required monthly payments, even assuming notice were contractually required.

The trial court criticized some of the bases on which LACDB accelerated the loan and commenced enforcement. (E.g., CT 1280:24-1281:1, 1282:13-22, 1283:3-11.) But it is beyond debate that by the time LACDB decided to accelerate, it had more than good reason to believe that the prospects of Summit's performing its payment and other obligations were severely impaired. That is enough to allow acceleration both under the loan agreement and under Commercial Code section 1208, which provides that acceleration requires "good faith belie[f] that the prospect of payment or performance is impaired."

U.S. v. Grayson (9th Cir. 1989) 879 F.2d 620 demonstrates how to apply this test. There, the U.S. Department of Commerce's Economic Development Agency loaned $2 million to a small corporation. The Agency accelerated the note after the borrower stopped making payments. At the time, the borrower was losing millions of dollars. The borrower challenged the acceleration, claiming that it occurred because an Agency employee sought to get a performance bonus. (*Grayson, supra*, 879 F.2d at p. 623.) Applying California law, the Ninth Circuit affirmed summary judgment for the Agency, noting that the acceleration decision was

"supported by objective business-related considerations," including the borrower's net loss, its admission that it would have difficulty making further payments, and its past failure to pay. (*Id.* at p. 623 & fn. 4.)

Summit's delinquency presented equally compelling "objective business-related considerations" justifying acceleration. Summit was deeply in arrears, and by its own admission was "loosing [*sic*] over $40,000 per week in cash flow." (Ex. 69/238.) No reasonable lender, and no reasonable trier of fact, could conclude that acceleration was not justified. The trial court erred as a matter of law in finding the contrary.

2. LACDB had no contractual obligation to assist Summit in obtaining an accounts receivable lender.

The trial court concluded that LACDB "refus[ed] to cooperate with Summit's attempts to obtain accounts receivable financing." (CT 1282:11-13.) But the loan agreement imposed no such obligation on LACDB.

The original loan agreement contemplated that Pine Cobble would continue to provide accounts receivable financing. (See Ex. 1/208, §§ 1.36, 3.5, 6.11.) That was why Pine Cobble was to hold a lien senior to LACDB's as to Summit's accounts receivable. (*Ibid.*) But once Pine Cobble's fraud came to light, this arrangement was no longer viable. The amended agreement eliminated the Pine Cobble exception, in favor of a much more limited exception to reflect Capital's partial interest in Summit's receivables as a result of the settlement. (See Ex. 2, § 3.) Beyond this, the loan agreement contained nothing that obligated LACDB to subordinate to any other lender, and it imposed no requirement that LACDB assist in securing alternative accounts receivable financing.

It is true that during discussions over what to do with Summit's defaults, the parties contemplated that Summit would obtain accounts receivable financing. But it is irrelevant whether LACDB agreed to subordinate to an accounts receivable lender, because Summit provided no consideration for any such agreement—it did no more than agree to come

into compliance with its existing obligations. (See *Auerbach v. Great Western Bank* (1999) 74 Cal.App.4th 1172, 1185 ["promising to do something one is already legally bound to do cannot constitute the consideration needed to support a binding contract"].)

The undisputed facts provide no basis for implying an obligation to subordinate to an accounts receivable lender. All Summit ever presented to LACDB was a letter from a factor inviting an application. (Ex. 66.) Summit apparently expected LACDB to provide a blanket subordination agreement—knowing nothing about the lender, the amount subject to subordination, or any of the terms and conditions of the prospective senior lien. No lender in its right mind would have done that. It is therefore impermissible for any court to imply an obligation to do so. (See *Pacific Gas & Electric Co. v. Superior Court, supra,* 15 Cal.App.4th at p. 608 ["a promise can be implied only where it can be rightfully assumed that it would have been made if attention been called to it"].)

Nor did LACDB have any duty to assist Summit in obtaining alternative financing. Although we have found no California decision directly addressing this issue, it arose in *Creeger Brick & Building Supply, Inc. v. Mid-State Bank & Trust Co.* (Pa.Super. 1989) 560 A.2d 151. The plaintiff borrower asserted that the bank violated the covenant of good faith and fair dealing by failing to cooperate in the borrower's efforts to obtain supplemental financing. The trial court sustained the bank's demurrer, and the appellate court affirmed. It concluded that "a lender generally is not liable for harm caused to a borrower by refusing to advance additional funds, release collateral, or assist in obtaining additional loans from third persons." (*Id.* at p. 154.)

The same is true here. Although LACDB was willing to subordinate to an accounts receivable lender, it had no duty to do so. It therefore could not have had an obligation—express or implied—to provide a blanket subordination agreement that Austin could shop around, subordinating LACDB's interest at will on terms over which LACDB had no control.

3. LACDB could not be liable for the actions of a court-appointed receiver, and in any event res judicata bars any such claim.

After accelerating the loan, LACDB sought to protect its interest in the collateral for the loan—Summit's assets—by obtaining the appointment of a receiver, David Pasternak. (CT 180, 257.) The trial court found that "[t]he receiver's action, or more specifically inaction, led to the loss of Summit's assets in Mexico which were valued in excess of $7 million" (CT 1279:23-24), and it concluded that LACDB "proximately caused damage to Summit . . . by seeking and obtaining the appointment of a receiver . . . ." (CT 1283:12-16.)

The statement of decision suggests no legal basis for such a claim. The ordinary remedy for a receiver's negligence, and no more was claimed here, is to surcharge the receiver before his discharge under Code of Civil Procedure section 566, subdivision (b). That is why a receiver posts a bond—"to protect those who might suffer loss from his failure to discharge his duties and administer his business in accordance with law and properly account for funds coming under his control." (*Stewart v. State of California* (1969) 272 Cal.App.2d 345, 351; see CT 259 [Pasternak's bond].)

But even if there were some theoretical basis on which plaintiffs could hold LACDB responsible for Pasternak's alleged misfeasance, res judicata bars them from doing so now, because Pasternak's discharge conclusively resolved the claim against them.[9]

Directly on point is *Aviation Brake Systems, Ltd. v. Voorhis*, *supra*, 133 Cal.App.3d 230. There, a party affected by the receivership sued the receiver after he had been discharged, alleging that he "failed to discharge his duties faithfully as receiver in the prior action." (*Id.* at p. 233.) The

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[9] Res judicata may be raised for the first time on appeal where, as here, a judgment involving the same issues and parties becomes final during the appeal. (*Aronow v. LaCroix* (1990) 219 Cal.App.3d 1039, 1046.)

trial court sustained a demurrer based on res judicata, and the Court of Appeal affirmed, stating:

> "We conclude that the matters sought to be litigated in the present action were, could have been, or should have been litigated at the time the receiver's final report and account was approved, and that the court's order in the prior case approving the account, which has become final, may not be collaterally attacked in this proceeding." (*Id.* at p. 234.)

So, too, here. In their objections to Pasternak's motion, plaintiffs squarely placed in issue the propriety of Pasternak's conduct. By granting Pasternak's motion, the trial court just as squarely rejected their claims. There is accordingly now an adjudication—final and binding, because plaintiffs did not appeal—that "[a]ll of [Pasternak's] actions appear to have been proper and in the best interests of this receivership estate and in compliance with this Court's orders." (RJN Ex. 14.) This adjudication bars plaintiffs from urging that Pasternak's conduct "led to the loss of Summit's assets in Mexico." (CT 1279:24-25.)

4. LACDB did not violate the implied covenant of good faith and fair dealing.

The statement of decision recites a litany of actions by LACDB that the trial court found violated the implied covenant. (CT 1280-1281, ¶ 1.) We have shown in Section I.D.2. that nothing in the loan agreement allowed the trial court to base any liability on any failure by LACDB to perform an additional UCC search, to use its own funds to resolve the problems caused by Pine Cobble's fraud, or to provide Summit with assistance in obtaining accounts receivable financing. Urging this conduct as a violation of the covenant of good faith and fair dealing doesn't improve plaintiffs' case, because it did not deprive Summit of any contractual benefit to which it was entitled. (See § I.C.1.) We address the remaining breach-of-covenant claims below.

a. No breach by erroneous belief that assets had been moved to Mexico. The trial court found that LACDB's officers were wrong to believe that Summit used the loan proceeds in Mexico rather than in the zone, since an audit concluding otherwise was in the file. (CT 1280:21-24.) The fact is irrelevant. Even if LACDB officers harbored this erroneous belief, acceleration and foreclosure were independently justified on other grounds, including Summit's severe and increasing delinquency.

Nor are any motives or feelings of LACDB officers relevant. LACDB had the contractual and statutory right to do what it did, and it had no duty to like plaintiffs or to trust them. The duty of good faith and fair dealing turns on *objective* unreasonableness, considered in light of the contract's purposes; motive is irrelevant outside the tort context. (See *Carma Developers, Inc. v. Marathon Development California, Inc., supra,* 2 Cal.4th at p. 373 ["the covenant of good faith can be breached for objectively unreasonable conduct, regardless of the actor's motive"]; *U.S. v. Grayson, supra,* 879 F.2d at p. 623.)

b. No breach by failure to clarify what was meant by the "located in the zone" requirement. The trial court concluded that LACDB breached the agreement in various ways in connection with the question of when and how Summit was to be located in the zone. Among other things, the trial court found that LACDB "abused its power to specify terms" by failing to provide a clear definition of what it would mean for Summit to be "'located in the zone,'" that it "continually chang[ed] the definition of being located in the zone," and that it "fail[ed] to accept the signing of a lease as satisfactory compliance." (CT 1282:13-20.) None of this supports a breach of the implied covenant, for several independent reasons.

First, the loan agreement refutes the trial court's accusation of vagueness, because it is very specific about what it means to be "located in the zone." It requires that "Borrower shall have leased, purchased or otherwise procured the use of a warehouse in the Empowerment Zone, which, when operational, shall be used as Borrower's principal warehouse in Southern California." (Ex. 1/208, § 3.11.) Although LACDB did not

require compliance with the contract requirement that Summit satisfy this condition at the loan closing, the definition never changed.

Second, although the loan agreement did not provide a date by which a warehouse in the zone had to be "operational"—that is, when it would be "used as Borrower's principal warehouse in Southern California"—the law implies a reasonable deadline, in light of the purposes of the agreement and the parties' intentions. (See Civ. Code, § 1657 ["If no time is specified for the performance of an act required to be performed, a reasonable time is allowed"]; *City of Stockton v. Stockton Plaza Corp.* (1968) 261 Cal.App.2d 639, 643-646 [look to contract purposes and surrounding circumstances to determine "reasonable" time to satisfy condition precedent].)

Here, Summit agreed not only to have its main warehouse in the zone, but that within two years it would employ 71 persons, half of them zone residents. (Ex. 1/208, § 3.16.) These two commitments were the essence of the contract—and LACDB's *raison d'être*. Yet by the time LACDB accelerated, nearly half of the two years had elapsed, and everything Summit tried had failed. At most, it had rented space that it was not yet using and had not staffed, and not one zone resident was working there. Since Summit had easily had a "reasonable time" in which to comply with its obligations, LACDB's decision not to wait any longer could not be a breach of the covenant of good faith and fair dealing, and the trial court's finding that there was a breach cannot be upheld.

Summit may urge that it wasn't to blame for failing to locate in the zone more quickly, because the task turned out to be much more difficult than anyone expected. It doesn't matter. As Justice Mosk observed:

> "Fault, comparative or otherwise, generally does not matter under the law of contracts. What matters, rather, is performance. Hence, performance with fault is sufficient, and nonperformance without fault is not enough." (*Kransco v. American Empire Surplus Lines Ins. Co.* (2000) 23 Cal.4th 390, 413 (conc. opn. of Mosk, J.); see also *U.S. v. Grayson*, *supra*, 879 F.2d at p. 623, fn. 4.)

Regardless of its efforts, the fact remains that Summit's failure to move into the zone meant that LACDB was devoting $2.5 million of scarce lending assets to an enterprise that wasn't anywhere near serving the goals for which the loan was made and showed no promise of ever being able to.

Third, LACDB's decision to accelerate was justified as a matter of law regardless of whether it acted unreasonably as to the zone requirement. Independent of its contractual obligation to be up and running in the zone, Summit's other fundamental delinquencies impaired LACDB's prospects for repayment as a matter of law, fully justifying acceleration.

*c. **No breach by unfounded suspicions about Summit's use of loan proceeds.*** The trial court condemned LACDB for harboring unfounded suspicions about Summit's actions, as expressed in a letter to Summit from LACDB's attorneys. (Ex. 247.) The trial court found that several claims made in that letter "were not founded on reasonable fact, investigation, or logic, and . . . were specifically contrary to known facts and documents that were available in the Bank files." (CT 1280:25-1281:1.)

There is no question that several LACDB officers did not trust Summit and believed that Summit was moving assets to Mexico instead of investing in the zone. But even if these beliefs were completely wrong, or even if they were not genuinely held, LACDB was still justified in accelerating the loan for objective, business-related reasons whose existence is not open to debate, most importantly Summit's severe payment delinquencies.

The implied covenant cannot superimpose a subjective "good intent" qualification on a party's exercise of its rights without violating the rule that "[t]he covenant of good faith and fair dealing cannot impose substantive terms and conditions beyond those to which the parties actually agreed." (*Starzynski v. Capital Public Radio, Inc., supra,* 88 Cal.App.4th at p. 39.) The trial court erred as a matter of law in premising a breach on LACDB's subjective motives and beliefs.

d. No breach by failure to notify Summit that LACDB would enforce the terms of the loan agreement. The trial court concluded that in negotiating with Summit, LACDB "established a course of dealing that modified the loan documents, and upon which the debtor relied, and failed to give notice before demanding compliance with the original course of dealing." (CT 1282:2-6.) The trial court erred in concluding that a course of dealing could supersede the contract's express terms.

Under the loan agreement, Summit and Austin specifically agreed that "[n]o prior waiver by Lender, action or inaction by Lender, *nor any course of dealing between Lender and Borrower*, or between Lender and Guarantors, shall constitute a waiver of any of Lender's rights or of any obligations of Borrower or of Guarantors . . . ." (Ex. 1/208, § 11.14, emphasis added.) The agreement further provides that "[n]o alteration of or amendment to this agreement shall be effective *unless given in writing and signed by the party or parties sought to be charged or bound* by the alteration or amendment." (Ex. 1/208, § 11.1, emphasis added.) The trial court's conclusion that the parties' course of dealing changed the terms of their agreement cannot be squared with these express provisions.

Nor can the trial court's conclusion be reconciled with section 1205 of the Commercial Code:

> "The express terms of an agreement and an applicable course of dealing or usage of trade shall be construed wherever reasonable as consistent with each other; but when such construction is unreasonable express terms control . . . ." (Comm. Code, § 1205, subd. (4); see also *U.S. v. Grayson, supra,* 879 F.2d at p. 623 [course of dealing cannot supersede express terms of loan agreement under Commercial Code].)

Summit agreed to make monthly payments of $43,000 and agreed that LACDB need not give notice of monetary defaults. (Ex. 1/208, §§ 9.14, 10.) Austin admitted there were no written modifications to these terms—in fact, he was still requesting a modification in the payment schedule right up to the acceleration. (RT 1685-1687; Ex. 69/238.) These

express provisions controlled from the time the loan was made until acceleration, and they preclude implying any obligation by LACDB to provide notice that it would invoke its rights under the loan agreement.

F. Error In Any Of The Trial Court's Findings Of Liability Requires Reversal.

As we have seen, the judgment rests on three legs: the trial court's invented "workout" mode; breach of contract in connection with the loan's funding; and breach of contract in connection with Summit's default. If any one of these legs fails, the judgment cannot stand. That is because each is essential to the judgment.

This is particularly true of the supposed pre-delinquency breaches. The trial court found that the Pine Cobble affair was the underlying cause of all of Summit's problems, and that its resolution involved breaches by LACDB. For example, after noting that Capital's involvement "resulted in a confusion affecting Summit's customers and caused a further cash flow problem" that led to Summit's delinquencies (CT 1277:1-2), the trial court found that "[t]he Bank proximately caused damage to Summit beginning on September 5, 1997 as a direct result of its actions regarding the UCC debacle" (CT 1283:12-14). It further found that Summit's failure to make timely payments "resulted directly from actions and breaches by the Bank and is legally excused" (CT 1282:28-1283:1; see also CT 1282:6-13), a description that can only refer to the Pine Cobble series of events. And only a belief that LACDB's contract breaches began with the Pine Cobble affair could possibly support the trial court's decision to measure damages by Summit's value on the date the loan funded.

A judgment wrong in any fundamental premise must be reversed, even if the evidence might otherwise support the judgment. That is the teaching of *Potter v. Firestone Tire & Rubber Co.* (1993) 6 Cal.4th 965. There, our Supreme Court reviewed a judgment against Firestone for intentional infliction of emotional distress arising from toxic waste disposal.

It found that "it is ambiguous whether the lower courts determined that Firestone's conduct was directed at these particular plaintiffs," a finding that the Court held was required for liability. (*Id.* at p. 1002.) The Court held that this ambiguity also required reversal of the punitive award, even though the award was independently supported by substantial evidence. The reason, the Court explained, was that the trial court *might* have based the punitive damages on a theory as to which it *might* not have made the necessary findings:

> "[B]ecause the trial court was of the view that Firestone's conduct constituted intentional infliction of emotional distress when it assessed punitive damages against Firestone, and might not have made the award or might have awarded a lesser sum had it not made that finding, that aspect of the judgment should also be reversed." (*Id.* at p. 1004.)

Although the context is different, the principle is the same here. The components of the judgment are interdependent, and it is impossible to know how the trial court would have evaluated the case if it had to do so without any one of the three main components of the judgment. Reversal is the only proper remedy.

II.

SINCE THE TRIAL COURT BASED ITS DECISION SOLELY ON BREACH OF CONTRACT AND AUSTIN WAS NOT A PARTY TO THE LOAN AGREEMENT, THE JUDGMENT IN HIS FAVOR ON THE COMPLAINT MUST BE REVERSED.

Having found a breach of contract by LACDB, the trial court did not consider plaintiffs' other claims, ruling that its decision rendered them "moot." (CT 1266:21.) But even though Austin was not a party to the Summit-LACDB loan agreement (see Ex. 1/208), the trial court unaccountably awarded judgment in his favor as well as Summit's. There is no basis for such a result.

"Someone who is not a party to the contract has no standing to enforce the contract or to recover extra-contract damages for wrongful withholding of benefits to the contracting party." (*Hatchwell v. Blue Shield of California* (1988) 198 Cal.App.3d 1027, 1034.) It doesn't matter that Austin is Summit's sole shareholder; the same principle applies. Austin would only have an individual cause "where it appears that the injury resulted from the violation of some special duty owed the stockholder by the wrongdoer and having its origin in circumstances independent of the plaintiff's status as a shareholder." (*Nelson v. Anderson* (1999) 72 Cal.App.4th 111, 124, internal quotation marks omitted.) There is no hint in the statement of decision that the trial court found either a special duty or a violation of it.

Although there was a separate contractual relationship between Austin and LACDB in the form of the loan guaranty Austin signed (Ex. 3), the statement of decision says nothing about it except to note that LACDB sued on it (e.g., CT 1267:13-14).

There being nothing whatever in the statement of decision to support any kind of liability to Austin, the judgment in his favor cannot stand.

III.

THE TRIAL COURT FAILED TO WEIGH THE DAMAGES EVIDENCE, WHICH IN ANY EVENT DOES NOT SUPPORT THE $7 MILLION AWARD.

Even though LACDB loaned Summit only $2,500,000, and even though Summit's total investment in the zone was only $65,000 (see RT 1245), the trial court held LACDB liable for $7.2 million, Summit's purported net worth when the loan agreement was signed (CT 1280). Apart from whether this award is supported by substantial evidence, its appropriateness depends entirely on the trial court's finding that LACDB's breaches of contract began when the loan funded. We have shown that there is no basis for that finding. Since the theory underlying the damages award is flawed, the damages award cannot stand even if the Court finds that Summit proved some other basis of liability. (See § I.F., *ante*.)

But the award is not supported by substantial evidence. And even more problematic, the statement of decision shows that the trial court did not weigh what evidence there was.

As Summit urged (RT 6124-6125), the trial court based its damages calculations on Exhibit 218, a LACDB document that summarized Summit's financial condition as of September 30, 1997. The document reflected no analysis by LACDB, which "took this information off of Summit's financial statements and put it into the computer program." (RT 2208; see Ex. 60, Bates 373-374 [Summit balance sheet showing the same figures].)

In its statement of decision, the trial court characterized this "analysis of Summit" as "unrebutted." (CT 1280:1.) Unrebutted? LACDB's accounting expert, Jonathan Hainer, was on the stand for two days, and one of the things he did was tear the analysis to pieces. (RT 5401-5449.) After the fact, at the hearing on the post-trial motions, the trial court said it was "not sufficiently persuaded" by Hainer. (RT2 8;

see RT2 14-15.) But the statement of decision is where the trial court was supposed to state the basis for its analysis—particularly since LACDB specifically asked for details on the calculation of damages (CT 1173) and directly asked the court how could state that the evidence was "unrebutted" in light of Hainer's testimony (CT 1232-1233).

This Court cannot presume that the trial court disbelieved Hainer's testimony if the statement of decision suggests that the trial court didn't consider it at all. As the court observed in *Estate of Larson* (1980) 106 Cal.App.3d 560, 567, the substantial evidence rule "operates only where it can be presumed that the court has performed its function of weighing the evidence. If analysis of the record suggests the contrary, the rule should not be invoked." (See *Gardner v. Superior Court* (1986) 182 Cal.App.3d 335, 339 ["It is the judge's responsibility to consider and weigh all the evidence and argument and make a reasoned choice."].) The trial court's failure to perform this essential function here compels reversal.

But regardless of what the trial court did, Summit's financial statements did not constitute substantial evidence of Summit's value.[10]

Summit stipulated that its financial statements were not prepared in accordance with generally accepted accounting principles (RT 5428), and Hainer, LACDB's expert, testified that they were "riddled with egregious errors." (RT 5293.) These included Summit's failure to include accumulated depreciation on its aging equipment, which inflated Summit's assessment of its net worth by as much as $4 million. (RT 5404-5407, 5409, 5420; see also RT 5421-5423, 5448-5449.)

Summit called no expert in response. Instead, it called a percipient witness, Robert Bradach. As an accountant for Summit's predecessor, he

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[10] Plaintiffs will doubtless argue that there was other evidence that could have supported the $7.2 million valuation, but that is irrelevant in light of the fact that the trial court relied on Exhibit 218. (See *Loth v. Truck-A-Way Corp.* (1998) 60 Cal.App.4th 757, 768, fn. 12, 769 [damage award reversed where jury considered improper damages evidence, even though substantial other evidence supported the award].)

was familiar with Summit's accounting software, but he had no personal knowledge of Summit's finances as of the time of the relevant events and had last worked for the company in 1995. (RT 5713-5714.) The best he could say was that from his historical knowledge of the company and its accounting system, "the Summit balance sheet"—with no particular balance sheet identified—"appears to be a fair representation of the assets, liabilities, and equity of the company." (RT 5735.) That conclusion, so far divorced from personal knowledge and expertise, is nothing but a "bald assertion" that cannot rise to the level of substantial evidence. (*Roddenberry v. Roddenberry* (1996) 44 Cal.App.4th 634, 654.)

But disputes over accounting techniques pale next to Summit's own admissions of its desperate, on-the-brink financial condition in September of 1997. It was *Austin* who said on August 28 that Summit "will not be able to meet it's [*sic*] current obligations under it's [*sic*] current circumstances." (Ex. 20/206.) It was *Austin* who said on September 9 that "[w]e will be out of business this week if we are not funded today" (Ex. 29), and who "wasn't lying" when he made that statement (RT 1574). And it was *Summit's own income statement*—part of the very financial statement LACDB used to prepare its loan evaluation (Ex. 218), on which the trial court based its damages finding—that showed Summit was $585,000 in the hole by the end of September 1997. (Ex. 60, Bates 375; compare Ex. 218, 9/30/97 income statement.) In the face of these admissions, no reasonable trier of fact could conclude that Summit's *net worth* was over $7 million when the LACDB loan funded.

So—there was no weighing of evidence, and no substantial evidence to be weighed. The trial court's failure to weigh the evidence requires a new trial on damages. But if this Court agrees that there was no substantial evidence of damages, it should reverse with directions to enter judgment for LACDB, because plaintiffs are not entitled to retry anything they failed to prove when they had the opportunity. (*McCoy v. Hearst Corp.* (1991) 227 Cal.App.3d 1657, 1661.)

IV.

THERE IS NO LEGAL BASIS FOR THE $2 MILLION AWARD OF PREJUDGMENT INTEREST.

The judgment includes over $2 million in prejudgment interest accruing from September 5, 1997, the date of the loan agreement. (CT 1261.) There is no legal basis for the award, because:

- The trial court improperly used interest as a substitute for calculating lost profits, as to which there was no evidence. No law allows an award of interest for this purpose.
- Even assuming the trial court intended to rely on Civil Code section 3287—the only permissible basis for an interest award here—the requirements of that statute could not be met, because there was never any certainty as to the amount of damages attributable to LACDB's actions.

The trial court therefore abused its discretion in awarding interest. Even if the damages award is affirmed, the interest award cannot stand.

A. There Is No Legal Basis For Awarding Interest In Lieu Of Lost Profits.

Civil Code section 3287 is specific about when a court may award interest in a breach-of-contract dispute. The court must award interest when damages were certain or capable of being made certain (subd. (a)), and it has discretion to award interest from a date no earlier than the filing of the complaint (subd. (b)).[11] The trial court did not purport to rely on

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[11] Section 3287 states:

"(a) Every person who is entitled to recover damages certain, or capable of being made certain by calculation, and the right to recover which is vested in him upon a particular day, is entitled also to recover interest thereon from that day, except during such time as the

(continued...)

either ground; its statement of decision does not even cite section 3287. Instead, it ruled:

> "[U]sing legal interest from September 5, 1997, is the most conservative, and the fairest means to measure the actual economic loss without getting into complex calculations that would become increasingly difficult and argumentative." (CT 1284:24-27.)

Here is what this really means: Without any of the avowedly necessary "complex calculations" and without any other relevant evidence, the trial court concluded that a company so troubled that it was on the brink of going out of business would nevertheless have generated a consistent 10% return on its net value over the next three years if LACDB hadn't enforced its loan obligations.

Let's put this finding in perspective. As a proxy for lost profits, the interest award assumes that Summit lost $720,000 per year in profits (i.e., 10% of the damage award), which must be *net* lost profits. (*Gerwin v. Southeastern Cal. Assn. of Seventh Day Adventists* (1971) 14 Cal.App.3d 209, 222-223.) To yield $720,000 in net lost profits, Summit's gross revenue would have to include at least an additional $516,000 to cover a year's worth of $43,000 monthly loan payments—i.e., total gross revenues of $1,236,000 ($720,000 + $516,000 = $1,236.000). Now, suppose there had never been a Pine Cobble problem or any threatened federal tax liens,

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[11] (...continued)

> debtor is prevented by law, or by the act of the creditor from paying the debt. This section is applicable to recovery of damages and interest from any such debtor, including the state or any county, city, city and county, municipal corporation, public district, public agency, or any political subdivision of the state.
> "(b) Every person who is entitled under any judgment to receive damages based upon a cause of action in contract where the claim was unliquidated, may also recover interest thereon from a date prior to the entry of judgment as the court may, in its discretion, fix, but in no event earlier than the date the action was filed."

and that the full debt to Pine Cobble was $1,279,000 as Austin testified at trial. (See RT 729.) In that case, Summit would have netted about $1,221,000 from its $2,500,000 loan. But since Summit would have had no working capital besides those net loan proceeds, achieving $1,236,000 in gross revenue would mean earning *over a 100% return on the $1,221,000 investment*—and that's without accounting for any other costs.

There are surely other ways of doing the math, but it doesn't matter. The trial court never even tried—it didn't want to "get[] into complex calculations that would become increasingly difficult and argumentative." (CT 1284:26-27.) But *that's the trial court's job*. "A judge has a duty to decide any proceeding in which he or she is not disqualified." (Code Civ. Proc., § 170.) The judge can't punt and allow entry of a judgment with such a palpably preposterous result.

B. Summit's Damages Were Not Capable Of Being Made Certain Without Adjudication.

We recognize that because the Court must make presumptions in favor of the judgment, it might be inclined to presume that the trial court did, in fact, intend to rely on section 3287. But that would not save the interest award, because it fails to meet the statute's requirements.

If the trial court did in fact rely on section 3287, it had to be relying on subdivision (a), for two reasons. *First*, subdivision (b) permits interest to accrue only from the filing of the complaint, while the trial court's award accrued from the date of the loan agreement. *Second*, subdivision (b) requires an exercise of discretion, and since the trial court did not purport to exercise its discretion under that subdivision, the Court cannot infer that it did. (*Estate of Larson*, *supra*, 106 Cal.App.3d at p. 567.)

But subdivision (a) does not permit the award. It entitles a judgment winner to prejudgment interest only when the amount of damages is "certain, or capable of being made certain by calculation" before the trial

court adjudicates the amount of damages and enters its judgment. (§ 3287, subd. (a).) Summit's claims never came close.

The statement of decision acknowledges as much when it notes that the plaintiffs presented "[a]t least three different methods of analyzing the value of this loss." (CT 1284:6-8; see CT 476 [complaint alleged $50 million in damages]; RT 5859, 6123 [Austin valued business at $14 million], RT 6124 [Summit's internal financial statements showed $6.6 million].) Rather, this was the classic situation in which "the amount of damage, as opposed to the determination of liability, depends upon a judicial determination based upon conflicting evidence and is not ascertainable from truthful data supplied by the claimant to his debtor." (*Wisper Corp. v. California Commerce Bank* (1996) 49 Cal.App.4th 948, 960, internal quotation marks omitted.) Thus, "where the amount of damages cannot be resolved except by verdict or judgment, prejudgment interest is not appropriate." (*Ibid.*)

Failure to adhere to these rules is an abuse of discretion. (See *Bullis v. Security Pac. Nat. Bank*, *supra*, 21 Cal.3d at p. 815.) The trial court indisputably abused its discretion here. There is no basis for a retrial; the interest component of the award must be vacated.

V.

THE TRIAL COURT ABUSED ITS DISCRETION IN AWARDING $2.4 MILLION IN ATTORNEY'S FEES.

The attorney's fee award bears no more resemblance to the evidence and the law than the improper award of interest. Although a trial court has broad discretion in this area, its discretion "may not be exercised whimsically, and reversal is required where there is no reasonable basis for the ruling or when the trial court has applied the wrong test to determine if the statutory requirements were satisfied." *(Ramos v. Countrywide Home Loans, Inc.* (2000) 82 Cal.App.4th 615, 621, internal quotation marks

omitted; see also *Heppler v. J.M. Peters Co.* (1999) 73 Cal.App.4th 1265, 1296 [applying standard to award of fees under Civil Code section 1717].)

The criteria for an award of fees under Civil Code section 1717 are: (1) the number of hours reasonably spent; (2) the reasonable hourly rate; (3) the novelty and difficulty of the issues; (4) the skill displayed in presenting them; (5) the preclusion of other employment by the attorney; and (6) the contingent nature of the fee award. (*Vella v. Hudgins* (1984) 151 Cal.App.3d 515, 521.) However, as our Supreme Court recently reaffirmed, "'a computation of time spent on a case and the reasonable value of that time is fundamental to a determination of an appropriate attorneys' fee award.'" (*PLCM Group, Inc. v. Drexler* (2000) 22 Cal.4th 1084, 1095.) Thus, any fee awarded must bear some "reasonable relationship" to the lodestar figure and to the purpose of the fee-shifting statute. (*Press v. Lucky Stores, Inc.* (1983) 34 Cal.3d 311, 324.)

The trial court's arbitrary—indeed, punitive—$2.4 million award ignores these principles.

A. The Lodestar Calculation Is Not Supported By Substantial Evidence.

Ordinarily, a party seeking to recover a reasonable fee submits evidence of the time counsel spent on the matter, supported by some credible method of recording time, plus evidence of counsel's hourly rate.

Plaintiffs' motion for fees offered nothing of the sort.

Instead of providing evidence of the time he spent, plaintiffs' counsel declared that he did *not* keep track of his time and that he "ha[s] *no idea* how many total hours [he] spent on this matter." (CT2 17:18, emphasis added.) Although he conjectured that he spent "at least half" of his working time on the Summit matter, totaling 2,500 hours (*id.* 17:20-21), no rational trier of fact could believe this. It would mean *billing* over 3,300

hours a year, or an *average* of 277 hours a month—*over nine hours a day, seven days a week, 365 days a year.*[12]

When LACDB presented this exorbitant result of counsel's estimate (CT2 66), counsel didn't disagree, but instead emphasized how hard he works—60-70 hours a week, every week, year in and year out, with no vacations. (CT2 519:18-24.) But that response gave the trial court even less basis for accepting counsel's estimate of billable hours. Since no lawyer can possibly charge for every working hour of every working day, counsel's estimate that he worked "6,240 hours over the past two years" (CT2 519:22-23) could not possibly translate into the pace of *billable* work he claimed. The trial court had no right to accept his estimate.

B. The Amount Awarded Bears No Reasonable Relationship To The Lodestar Number And Is Unsupported By Required Findings.

The trial court didn't stop at accepting Mr. Lewin's undocumented and incredible statement that he was billing 3,300 hours a year. It also nearly *quadrupled* his hourly rate, paying him almost $1,000 per hour—*a $2 million premium over his hourly rate.*

This four-times multiplier is virtually unprecedented in reported California decisions and is utterly unsupported in the record or the trial

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[12] Mr. Lewin said he spent "a minimum of 2,500 hours" on the case, which lasted 18 months from the filing of the complaint to the end of trial (August 27, 1998 to February 8, 2000), and that this was half of his time. (CT2 17.) That means he billed 5,000 hours in 18 months, which translates to over 3,300 hours per year or over 277 hours per month.

court's findings.[13] Indeed, much smaller multipliers have been consistently vacated despite much stronger showings than the one made here.[14]

This windfall is particularly unwarranted given LACDB's status as a taxpayer-funded, nonprofit institution. (See *Salton Bay Marina, Inc. v. Imperial Irrigation Dist.* (1985) 172 Cal.App.3d 914, 957 [noting that defendant is public entity in reversing award against it based on contingency agreement].)

Even if the unprecedented four-times multiplier were abstractly supportable, it still must be set aside because the trial court failed to make findings justifying the award. (See *Ramos v. Countrywide Home Loans, Inc., supra,* 82 Cal.App.4th at p. 629 [vacating award of multiplier due to lack of explicit findings based on evidence].)

For example, the trial court noted that the case "must have" precluded other work by plaintiffs' trial counsel. (RT2 31.) But plaintiffs presented no specific evidence of any work lost; the entirety of the evidence was the conclusory statement that "[m]y commitment to this case forced me to turn down several other matters, including cases against this Bank, that I

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[13] Our research has not disclosed a single reported California decision upholding a multiplier of four or higher under *any* fee-shifting statute. The only possible candidate is *Glendora Community Redevelopment Agency v. Demeter* (1984) 155 Cal.App.3d 465, decided by Division 4 of this Court. But the analysis in that case, particularly its reliance on the existence of a contingency agreement, has since been rejected by two other courts. (See *Salton Bay Marina, Inc. v. Imperial Irrigation Dist., supra,* 172 Cal.App.3d at p. 957 (Fourth Dist., Div.1); *People ex rel. Dept. of Transportation v. Yuki* (1995) 31 Cal.App.4th 1754, 1770-1771 (Sixth Dist.).)

[14] E.g., *Ramos v. Countrywide Home Loans, Inc., supra,* 82 Cal.App.4th 615 (reversing award of 2.5 multiplier because trial court had no reasonable basis in record and noting that "reasonable exercise of discretion will not allow [an effective $800/hour rate] except in truly pioneering and high risk cases"); *Weeks v. Baker & McKenzie* (1998) 63 Cal.App.4th 1128, 1174, fn. 23, 1176 (reversing 1.7 multiplier even where plaintiff had a 40% contingency agreement); *Flannery v. California Highway Patrol, supra,* 61 Cal.App.4th 629, 647 (reversing 2.0 multiplier).

otherwise would have handled." (CT2 18:23-25.) Similarly, the trial court's bare conclusions about the difficulty of the issues and the skill of counsel, to the extent they were articulated at all, were more than adequately accounted for in the lodestar. (RT2 30-31.)

Mere conjecture is not a sufficient basis for awarding a $2 million premium over the presumptively reasonable lodestar fee. The evidence and findings must be compelling to support such an extraordinary award. Their absence compels reversal.

CONCLUSION

The trial court seemed to feel it had to find a way to resurrect Summit's fortunes at LACDB's expense—"there was a wrong done to the plaintiff here, and I tried to fashion a remedy for that wrong." (RT2 16.) It had no right to do so. Neither the evidence nor the law permitted a finding of liability, and the award of interest and attorneys fees go far beyond even the semblance of faithfulness to legal principle.

The judgment should be reversed with directions to enter judgment for LACDB on both the complaint and cross-complaint, subject only to the determination of damages and attorney's fees on the cross-complaint. If the Court affirms the liability portion of the judgment, it should nevertheless reverse for a new trial on damages and with directions that plaintiffs cannot recover pre-judgment interest.

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Respectfully submitted,

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