Filed 9/28/18 Elysian Care Corp. v Lawndale Healthcare & Wellness Centre CA2/8

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION EIGHT

ELYSIAN CARE CORPORATION et al., Plaintiffs and Respondents, v. LAWNDALE HEALTHCARE & WELLNESS CENTRE, LLC, et al., Defendants and Appellants.	B281904, B283523 (Los Angeles County Super. Ct. No. BC471385)

CONSOLIDATED APPEALS from a judgment and postjudgment order of the Superior Court of Los Angeles County, Teresa Sanchez-Gordon, Judge. Reversed and remanded with directions.

Hooper, Lundy & Bookman, Amanda L. Hayes-Kibreab and Jonathan H. Shin, for Defendants and Appellants.

Ablon, Lewis, Bass & Gale, Jerald E. Gale and Lawrence J. Poteet, for Plaintiffs and Respondents.

INTRODUCTION

This lawsuit has several distinct components. The first involves voluminous and complex billing issues that arose after plaintiffs sold their skilled nursing facility to defendants; these issues were the subject of a special reference. The trial court eventually adopted the special master's "Determinations and Findings" in plaintiffs' favor, but declined to hold any hearings before doing so. The second aspect concerns attorney fees incurred by plaintiffs to ensure a promissory note, personally guaranteed by their principals, did not go into default. Over defendants' objections the trial court awarded plaintiffs these attorney fees as damages. Postjudgment, plaintiffs were awarded prevailing party attorney fees and costs. For the reasons that follow, we reverse and remand with directions.[1]

FACTUAL AND PROCEDURAL BACKGROUND

Plaintiffs in this action are Elysian Care Corporation (ECC), the former owner and operator of a licensed skilled nursing facility, and Lawndale Healthcare Enterprises, LLC (LHE), the former owner of the real property and improvements. The principals in these two entities, Robert and Cvia Bouskill, are not parties to the action.

On March 2, 2011, escrow closed on plaintiffs' sale of the business, improvements, fixtures, and real property to defendants Lawndale Healthcare & Wellness Centre, LLC (Lawndale); Lawnland, LLC (Lawnland); and the principal of

---

[1] Defendants appealed separately from the judgment and postjudgment order. We ordered the appeals consolidated for briefing, oral argument and decision.

these two entities, Kenneth H. Lehmann.[2] The sale was accomplished via an asset purchase agreement (APA).

When escrow closed, the real property was encumbered with two deeds of trust. The first secured a loan to plaintiff LHE from Pacific Western Bank (bank loan). The Bouskills were personal guarantors of this promissory note. Because the bank loan contained a " 'due on sale' " clause, defendant Lawnland purchased the real property " 'subject to' " it. Plaintiffs maintained a special account for the bank loan, and the APA provided defendants would directly deposit the monthly payment into that account to keep the bank loan current. The outstanding balance of the loan was approximately $1.1 million when escrow closed.

The second deed of trust secured an existing Small Business Administration (SBA) loan. The APA required LHE to pay off this loan and remove the encumbrance; LHE did so. In return, Lawnland signed a promissory note in LHE's favor (seller note) for the previous outstanding balance of the SBA loan, plus the prepayment penalty plaintiffs incurred to retire it. The seller note, in the amount of $592,134.83, was secured by a new second deed of trust (seller deed of trust).

Lawndale provided a limited liability company guaranty for the seller note, which was also personally guaranteed by Lehmann. Both guaranties extended to Lawnland's "obligations to pay in full the [bank loan]" and the guarantors further "promise[d] to pay, on demand . . . all reasonable costs and

---

[2] In the trial court, the parties occasionally varied the appellations for the entities. To avoid confusion, we will consistently refer to them as indicated above.

attorney's fees actually incurred in collecting the indebtedness or enforcing this Guaranty, regardless of whether or not an action is filed." A security agreement covering the assets of the business provided yet more security for the seller note.

The APA obligated defendants to pay off both the bank loan and seller note by December 15, 2011. Defendants had an option to extend the due date until March 15, 2012, provided they were not then in default.

When escrow closed, Lawndale was not licensed to operate a skilled nursing facility, nor did it possess its own Medicare and Medi-Cal provider numbers. Accordingly, the parties entered into a management agreement (MA) for the operation of the facility during the transition. The MA required Lawndale to assume responsibility for all billing, invoicing, and collection activities during this period, using ECC's provider numbers. Because of the typical lapse of time between providing services, billing, occasionally re-billing, and finally collecting fees, the MA required Lawndale to perform some of these activities for the benefit of ECC's account. Lawndale was responsible for keeping plaintiffs apprised of the status of these efforts.

Discord quickly surfaced between plaintiffs and defendants. ECC accused Lawndale of not timely processing claims payable to their account, resulting in some claims becoming time-barred. But plaintiffs' accountant discovered "an unprecedented number of claims" that ECC either failed to bill or billed incorrectly before the sale. As ECC was no longer operating the business, it relied on Lawndale to correct these oversights.

Lawnland was chronically late in its monthly debt obligations. The automatic transfer setup from defendants' work account to plaintiffs' account for payment of the bank loan never

materialized; and plaintiffs had to rely on defendants' mailing the monthly check in advance of the due date so it would be deposited in time for the payment. Time and again LHE stepped in and made the bank loan's monthly payment before receiving Lawnland's check to prevent a default on that obligation.

For their part, defendants asserted Medicare and Medi-Cal were making adjustments for earlier overpayments to plaintiffs by reconciling the accounts at the expense of defendant's receivables.

Plaintiffs initiated this lawsuit on October 12, 2011, seeking declaratory relief and damages based on the patient billing issues.[3] Lawnland paid the seller note in full in November 2011. By its terms, the seller note was not yet "satisfied" because the bank loan was still outstanding. The limited liability company and personal guaranties, as well as the security agreement, remained in place, and LHE did not reconvey the seller deed of trust.

Beginning with the January 2012 payment, Lawnland failed to deposit the monthly sum due on the bank loan. In February 2012, LHE commenced nonjudicial foreclosure proceedings on the seller deed of trust, the one that secured the seller note.

Plaintiffs also filed a first amended complaint on April 25, 2012, to add four causes of action—three of which are relevant

---

[3] The original complaint included seven causes of action: (1) breach of contract, (2) declaratory relief, (3) negligence, (4) fraud, (5) accounting, (6) unfair business practices, and (7) indemnity.

here.[4] In the eighth cause of action, plaintiffs sued defendants for breach of the APA and the seller note (although only Lawnland had signed the latter) based on defendants' falling behind on the monthly bank loan payment. The tenth and eleventh causes of action were against the guarantors for breach of their respective guaranties on the same theory.

Confronted with the nonjudicial foreclosure, defendants asked plaintiffs for a payoff demand statement (Civ. Code, § 2943). In early August 2012, plaintiffs provided a payoff demand statement in a form consistent with Civil Code section 2943. It included the unpaid balance, interest, and assorted fees related to the bank loan and sums for the advances plaintiffs made to keep the bank loan out of default, along with interest and late charges thereon. The payoff demand statement also included "Statutory Attorney Fees" (Civ. Code, § 2924c) and advised these were "actual fees due [that] can only increase by the amount of accruing interest," but were subject to change based on "any attorney[] fees that may be incurred prior to payment of this demand."

Plaintiffs intentionally omitted from the payoff statement demand more than $75,000 in attorney fees they claimed to have incurred to ensure the Bouskills never became liable on their personal guaranties of the bank loan and to set the stage for, and proceed with, the nonjudicial foreclosure. No evidence suggests plaintiffs ever told defendants the payoff demand statement was in any way incomplete.

---

[4] Plaintiffs voluntarily dismissed the ninth cause of action before trial.

Lawnland promptly paid in full plaintiffs' demand. The seller deed of trust was then reconveyed, and a termination of the UCC Financing Statement was filed. Plaintiffs retired the bank loan and the Bouskill guaranties were released. By their own terms, the APA was satisfied and the guaranties were extinguished without further action ("This Guaranty shall remain in effect until the [seller note] is paid in full to [LHE] and the [bank loan] is paid in full to the holder thereof and all liens and security interests pertaining to the [bank loan, e.g., the Bouskill guaranties,] are released.")

Turning their attention back to the billing issues, counsel recognized this case should proceed in a somewhat out-of-the box fashion based on the complexity of the patient billing issues, the voluminous Medicare and Medi-Cal billing records, and state and federal laws that prohibited a number of relevant documents from being removed from the facility. The stipulated solution was to stay most of the causes of action and embark on a special master/referee[5] journey to address the billing claims.

Counsel agreed to this procedure "in order to promote judicial economy and to conserve the valuable resources and time of the court and the parties, and to promote settlement and resolution of such issues without consuming undue attorney[] fees, court time and judicial resources." The stipulation contemplated the same individual would serve as both mediator and special master. It described the special master's role as "rendering the [a]ccounting and hearing the evidence to be

---

[5] The terms "special master" and "referee" are interchangeable. (*In re Marriage of Olson* (1993) 14 Cal.App.4th 1, 6, fn. 4.)

presented by the parties with regard to their respective contentions and disputes concerning the [a]ccounting issues." Although it would later become the subject of some contention, arguably the stipulation covered the first cause of action for breach of contract for allegedly failing to timely bill ECC claims; the second, for declaratory relief; the fifth, for an accounting; and the applicable affirmative defenses.

The stipulation included the following provisions:

> Upon the conclusion of such formal presentations of evidence and arguments by counsel to the Special Master, the Special Master shall thereupon issue a reasoned and detailed formal written set of "Determinations and Findings," which Determinations and Findings shall be promptly submitted to the parties and to the Court. The Determination and Findings, when so presented to the parties and to the Court shall, within 30 days of such presentation, be adopted by the Court and incorporated into any final judgment entered in this action, unless within 15 days of such presentation to the Court, one or more of the parties shall file written objections thereto and request that the Court set an evidentiary hearing or hearings as may be required in order to rule upon such objections. In the event any party shall file objections to the Determination and Findings as set forth herein, the Court shall thereupon set the matter for hearing at such time as the Court determines is proper, and the

> parties shall thereupon at such hearing be permitted to present such evidence to the Court concerning their respective objections, and any evidence in support of or in opposition thereto. The Court shall, after hearing such matters, then render its own independent determination with regard to the Accounting claims, and such determination by the Court shall be made a part of any final judgment entered in the action.

Paragraph 5 of the proposed order jointly submitted by counsel repeated, word-for-word, the language reproduced above. The judge signed the parties' order without making any changes.

Several months later, the trial court appointed the Honorable Ann Kough (ret.), affiliated with a private mediation firm, to serve as the mediator/special master.[6]

Judge Kough's assignment—including mediation efforts, discovery, evidentiary hearings with witness testimony, and legal briefing—spanned several years. She issued "Determinations and Findings" (the report) on July 23, 2015. There, she found the disputed accounting issues involved "approximately 43 files." The special master made a number of factual findings and legal conclusions. She determined plaintiffs' damages for the accounting claims were a net $447,705.87, calculated as follows:

---

[6] The order in the appellate record is unsigned and the space for Judge Kough's name is blank. But a June 6, 2014 stipulation advised that after unsuccessful mediation efforts, the parties participated in extensive discovery pursuant to Judge Kough's order, "including review and photocopying of more than 46,000 documents, and review of the same by the parties' respective medical billing experts."

$461,151.67 in lost revenue as a result of the breaches by Lawndale and Lawnland, less $13,445.80 that ECC owed Lawndale in offsets for previous overpayments. She concluded these recommendations resolved the first, second, and fifth causes of action for breach of contract, declaratory relief, and an accounting.

Defendants promptly returned to the trial court with objections to the special master's report and a request for "an evidentiary hearing or hearings in order to rule on such [o]bjections." Defendants challenged a number of evidentiary rulings and faulted the report for ignoring evidence favorable to them, making findings unsupported by the evidence, and failing to make findings on a claim-by-claim basis. Defendants did not, however, challenge the special master's stated scope of her assignment, except to note she did not do enough: "The findings are deficient in that they lump all patient claims together and do not make any specification as to which are illegal. There is no reference to . . . [d]efendant's listing of the patient claims, which if billed would constitute false claims under . . . the False Claims Act." Almost six months of procedural wrangling followed. The details are not necessary to resolve the appellate issues, but may be summarized as follows: Defendants insisted the stipulated order required the trial court, not the special master, to conduct further hearings on defendants' objections. There were no reporter's transcripts or other suitable substitutes for the proceedings before the special master, however, so the trial court referred the hearing on defendants' objections back to her. Defendants initially declined to participate in any further hearings before the special master. Defendants then indicated they would participate, but the special master advised they had

not paid their fees to do so. Defendants disagreed and said the fees were paid. Bottom line: There was no hearing before the special master on defendants' objections. On January 11, 2016, the special master issued a ruling that addressed and overruled each objection.

In the meantime, plaintiffs requested a preferential trial setting on the APA, seller note, and guaranty claims because the Bouskills are elderly. The trial court was reluctant to proceed with those claims until the accounting issues were resolved. Defendants were reluctant to proceed until their "fundamental right to a noticed hearing and the opportunity to present evidence, written and oral argument . . . as required by paragraph 5 of the original Bifurcation Order" was acted upon.

Defense counsel raised the issue of a trial court hearing on the special master's report at every opportunity. In November 2015, he told the judge, "The only issues that remain now are legal issues. They're not factual issues. We are not going to re-examine all the accounts. [¶] If you look at the objections themselves, they are primarily legal objections. Namely, the False Claims Act; namely, the fact [that defendants desire to reopen to present evidence of an insurance company's subsequent denial of one of the disputed claims]."

At the June 6, 2016 hearing, the following colloquy occurred: "[Defense counsel]: . . . we don't look at the special master's findings as res judicata. Those are merely recommendations. And technically, as we brought up before, the court— [¶] The court: They are recommendations. [¶] [Defense counsel]: The court has to have an independent hearing on those issues. [¶] The court: I'm not going to do that. [¶] [Plaintiffs'

counsel]: We've already done that. [¶] . . . [¶] The court: The court has already ruled on that issue."

When the matter was called for the court trial on July 11, 2016, the judge advised defense counsel: "Before you're heard, Mr. Abramson, I want to be clear that we are not—and the court has ruled on more than one occasion. And I understand, Mr. Abramson, your efforts to try to convince the court otherwise, and you're in your total right to do that, but . . . this court has been very clear regarding its position on conducting evidentiary hearings regarding [the special master]s findings and . . . determination. The court has said no. It will not do it." A bit later, the judge added, "I intend to adopt [the special master's] findings and determinations. I don't intend to reject any part of it."

With that admonition, attention turned to the remaining causes of action.[7] The eighth, tenth, and eleventh causes of action in the first amended complaint sought "damages in an amount equal to the advances [LHE] was required to make for . . . the [bank loan] . . . plus interest on said advances . . . , plus accrued late charges, along with an amount equal to the unpaid principal balance of the [bank loan]" as well as all reasonable costs and attorney fees actually incurred to collect defendants' debt and enforce their obligations under the APA and guaranties. The prayer sought attorney fees as costs.

In apparent acknowledgement that defendants paid the debt four years earlier and all securities and liens had been released, plaintiffs advanced the theory that they were entitled to

---

[7] Plaintiffs previously dismissed without prejudice a handful of other claims.

additional damages in the sum of $81,515, representing what they called "extraordinary" legal fees incurred to keep the bank loan from going into default after the sale to defendants and to protect the Bouskills from liability on their personal guaranties. The sole witness for this aspect of plaintiffs' case was Robert E. Lewis, the attorney who represented them in the sale transaction and whose firm has represented plaintiffs throughout these proceedings.

Bills from Lewis's firm received into evidence to support the $81,515 damages' claim spanned the period from shortly after the sale closed—months before the lawsuit was filed—to a date after the bank loan and associated fees and costs were paid. The billing attorneys were Lewis and his partner, Jerald Gale, one of plaintiffs' litigation/trial attorneys. The bills included a wide range of services the law firm performed related to the sale, post-sale operation of the business, and protection of the Bouskills' guaranty of the bank loan. For example, Lewis billed for his efforts to set up accounts that were to be used for the bank loan payments and his creation and review of a multitude of documents and e-mails in the months before the lawsuit was filed. Lewis and Gale each billed for conferences between the two of them and for their individual reviews of what appeared in numerous instances to be the same documents. Lewis testified, "The most important thing from [the Bouskills'] point of view was to get that . . . million dollar-plus [bank loan] paid off so that the guaranties were released." Lewis offered no testimony concerning what was meant by "extraordinary attorney fees" or what was "extraordinary" about the services his firm performed.

When plaintiffs rested, defendants moved for judgment under Code of Civil Procedure section 631.8.[8] The trial court invited supplemental briefing, took the matter under submission, and denied the motion. Defendants presented no evidence on the attorney fees issue.

As the trial court previously indicated it would do, it adopted without change the special master's report. It awarded plaintiffs an additional $81,515 in attorney fees as damages. Judgment was entered in plaintiffs' favor on all the remaining causes of action. Plaintiffs prepared an amended statement of decision, which the trial court signed without any revisions. Plaintiffs were declared the prevailing parties.

Postjudgment, plaintiffs filed a memorandum of costs in the sum of $42,313.15. Defendants' motion to strike or tax costs was granted in part, leaving plaintiffs with $16,896.67 in costs. To this amount, however, the trial court added $189,599.07 in "non-statutory fees," explaining "[p]laintiffs did not identify—in the motion [for attorney fees and additional costs] or in the declarations—the exact components, which make up the non-statutory fees requested, although some are clear." This was a reference to expert witness fees that had not been listed in plaintiffs' memorandum of costs. The trial court awarded plaintiffs $934,276 in prevailing party attorney fees. The total attorney fees and costs award was $1,140,771.74.

Defendants' motion for new trial was denied. They timely appealed from the judgment and postjudgment award of attorney fees and costs.

---

[8] All further undesignated statutory citations refer to the Code of Civil Procedure.

DISCUSSION

I. Special Reference — Accounting Issues

The issue presented in this portion of the appeal is whether the trial court prejudicially erred in declining to hold a hearing on defendants' objections to the special master's report and plaintiffs' opposition to them. We conclude it did, and reversal is compelled.

A. The First Reference

The trial court, in its amended statement of decision, explained the special master's assignment was a special reference under section 638, subdivision (b). Plaintiffs, in their brief to this court, described a hybrid: "The reference was a consensual 'general' reference pursuant to which the referee's [report] would be automatically incorporated into the final judgment, *unless* objections were timely filed . . . [and then the report] would be subject to review by the trial court." Defendants maintained the entire process was in excess of the trial court's jurisdiction because their stipulation to a special reference did not include a "discussion of matters of liability or findings of law. [¶] Yet, the Special Master proceeded to decide the entirety of the [first, second, and fifth] [c]auses of [a]ction, as well as [defendants'] defenses thereto."

Counsel's agreement to refer the accounting issues to a special master and the trial court's order constituted a special reference pursuant to section 638, subdivision (b).[9] The initial

---

[9] If the court "finds a reference agreement exists between the parties," it may appoint a special master (sometimes also called a referee) "[t]o ascertain a fact necessary to . . . determine an action or proceeding." (§ 638, subd. (b).)

special reference was certainly well within the trial court's jurisdiction and discretion.

B. Lack of Precision as Presaging Problems

Among other requirements, stipulations for the appointment of a special master must "[c]learly state whether the scope of the requested reference includes all issues or is limited to specified issues." (Cal. Rules of Court, rule 3.901(b)(1).) The court's order must also specify "[w]hether the scope of the reference covers all issues or is limited to specified issues." (Cal. Rules of Court, rule 3.902(2).) With hindsight and the passage of five years, the wisdom of these rules cannot be overstated.

Here, the order of reference did not identify the statute under which it was made, nor the causes of action that would fall under the special master's purview. But when counsel stipulated to the special reference, they indisputably agreed the special master was not limited simply to rendering an accounting. The stipulation provided the special master would oversee discovery and conduct "formal presentations of evidence and arguments by counsel" as they pertained to all the "[a]ccounting claims." This included "hearing the evidence to be presented by the parties with regard to their respective contentions and disputes concerning the [a]ccounting issues," after which the special master was required to "issue a reasoned and detailed formal written set of 'Determinations and Findings.' "

After being involved in this litigation for two years, first as a mediator and then as a special master, the special master reported she still was "not certain exactly what the 'Accounting Claims' consist of, since that term was not defined in the Order." She concluded, however, her assignment was broader than the

fifth cause of action seeking an accounting: "The Special Master does not believe, nor did the parties act as if, this was the entirety of the Accounting Claims . . . . [¶] Based on the submissions by and conduct of the parties, the Special Master determines her assignment to be to hear and decide all patient claims for which Plaintiffs allege that Defendants beached a duty to bill and collect on Plaintiffs' behalf and Defendants' affirmative defense of offset for patient claims Defendants assert Medicare or Medi-Cal recouped monies from Defendants for claims previously paid to Plaintiffs and payments received by Plaintiffs but earned by Defendants." In fact, she determined all the discovery the parties conducted under her watch rendered the accounting itself moot. No party challenged in the trial court the special master's practical and transparent description of her assignment.

Having established the parameters for the assignment, the special master proceeded to make factual findings and determinations. Of particular significance, she found Lehmann was not a proper defendant on the accounting claims "unless the [trial] [c]ourt finds [him] to be an alter ego of Lawndale and/or Lawnland." She concluded Lawndale violated the MA by failing to communicate to ECC that a number of pre-sale billings were deficient and needed to be rebilled for ECC's benefit and by not providing ECC with access to the facility's books and billing records to verify defendants' compliance with the terms of the MA. Addressing the claims that were ECC's fault, the special master found the parties orally modified the MA to require Lawndale to assume responsibility for "perform[ing] all of the billing that was not already time barred," with ECC promising to reimburse Lawndale for the added expense. She rejected defense evidence that any attempts to bill or and re-bill for those claims

would constitute fraud or violate the federal False Claims Act.[10] She further found plaintiffs detrimentally relied on defendants' agreement to bill the disputed claims and faulted defendants for not advising plaintiffs it would not honor the oral agreement.

C. Objections to the Special Master's Findings and the Second Reference

Although counsel earlier appeared to be in agreement concerning the scope of the reference, defendants' perspective changed once the special master issued her report. But even at that point, some two years after the special reference was ordered, there was ample opportunity for a course correction. In the case of a special reference, "the decision of the referee . . . is only advisory. The court may adopt the referee's recommendations, in whole or in part, after independently considering the referee's findings and any objections and responses thereto filed with the court." (§ 644, subd. (b).)

To that end, after defendants received the special master's report, they filed written objections in the trial court and asked for an evidentiary hearing, as the stipulated order entitled them to do. When advised there were no reporter's transcripts of the hearings before the special master, the trial court referred the objections, back to the special master.[11] This referral was

---

[10] The special master also noted "[d]efendants never raised the alleged issues of fraud and illegality until after this action was commenced."

[11] Defense counsel argued in the trial court that the objections and remaining issues were legal in nature: "The only issues that remain now are legal issues. They're not factual issues. We are not going to re-examine all the accounts. [¶] If you look at the objections themselves, they are primarily legal

consistent with the stipulated order that gave the trial court authority to "set an evidentiary hearing or hearings as may be required in order to rule upon such objections."

This time, there was no stipulation for a referral to the special master to consider the objections; and this became a special reference under section 639, subdivision (a)(1), (2), and/or (3).[12] Referring the matter back to the special master to consider the defense objections also was within the trial court's jurisdiction and discretion. (*Jovine v. FHP, Inc.* (1998) 64 Cal.App.4th 1506, 1521.)

D. The Failure to Conduct A Hearing

The trial court erred, however, when it declined to hold a hearing of any kind after the special master reported on defendants' objections. It is well settled that trial courts need not hold hearings on a discovery referee's recommendations or the objections to them. (*Marathon Nat. Bank v. Superior Court* (1993) 19 Cal.App.4th 1256, 1261.) The trial court's reliance on *Marathon* to deny the parties a hearing was misplaced; this was not a discovery reference.

---

objections. Namely, the False Claims Act; namely, the fact [that defendants desire to reopen to present evidence of an insurance company's subsequent denial of one of the disputed claims]."

[12] Without the consent of the parties and on its own motion, a trial court may appoint a special master in the following circumstances: (1) to examine a long account and "hear and decide the whole issue, or report upon any specific question of fact involved;" (2) to provide information to the court before judgment; or (3) "[w]hen a question of fact . . . arises . . . in any stage of the action." (§ 639, subd. (a)(1)-(3).)

Rather, the stipulated order clearly spelled out the procedures the trial court and parties were obliged to follow once the special master reached her decision: If there were no objections, the trial court was required to incorporate the special master's report into the final judgment. If, on the other hand, one or both parties filed objections, the trial court was required to "render its own independent determination with regard to the Accounting claims," but only *after* the parties had the opportunity to "present . . . evidence to the [trial court] concerning their respective objections, and any evidence in support of or in opposition thereto."

The stipulated order did not preclude the trial court from referring defendants' objections back to the special master, but it also did not give the trial court discretion to delegate to the special master the authority to rule on defendants' objections. The special master's conclusions as to the objections could only be recommendations. The trial court was still required to hold its own hearing before it could rule on the objections and before it could "render its own independent determination with regard to the Accounting claims."

Although counsel agreed the special master resolved most, if not all, of the fact issues, no evidence was ever received in the trial court on the accounting issues, nor did the parties argue any of the legal issues (e.g., oral modification of the MA, False Claims Act) because the trial court, in contravention of the parties' express agreement and its own order, entered judgment on the special mater's report without the requisite hearing on defendants' objections.[13] The trial court was not entitled to enter

---

[13] The judgment even provided for prejudgment interest on these causes of action "from July 17, 2015, the date on which [the

judgment until after it conducted a hearing on the objections and opposition to them. (*De Guere v. Universal City Studios, Inc.* (1997) 56 Cal.App.4th 482, 505.)

That portion of the judgment pertaining to the accounting issues must be reversed and remanded for a hearing or hearings consistent with the parties' stipulation and the trial court's order.[14]

II. Attorney Fees as Damages

Defendants attack this portion of the judgment on four fronts. They argue the attorney fees awarded as damages constituted an impermissible deficiency judgment; contractual attorney fees, while recoverable as costs, are not damages; plaintiffs could not claim these attorney fees after intentionally

---

special master] issued her 'Determinations and Findings' . . . which . . . have been adopted as the [c]ourt's [s]tatement of [d]ecision."

[14] At oral argument, defense counsel insisted their clients were entitled to essentially scrap the special master's work and begin the evidentiary process anew. That was not what the parties bargained for, however; and nothing in the trial court's order or in any proceedings conducted to date entitles defendants to that remedy on remand. The parties' stipulation and the trial court's ensuing order were specific. The parties have the right to a hearing before the trial court on the objections. At that hearing, they are to "be permitted to present such evidence to the [trial] [c]ourt concerning their respective objections, and any evidence in support of or in opposition thereto. The [trial] [c]ourt shall, after hearing such matters, then render its own independent determination with regard to the Accounting claims, and such determination by the Court shall be made a part of any final judgment entered in the action."

omitting them from the payoff demand statement; and the trial court abused its discretion in finding plaintiffs incurred any "extraordinary" attorney fees.

A. There Was No Deficiency Judgment

Defendants' first argument is easily resolved. The seller note was "given as consideration for a business loan arising pursuant to that certain [APA]." The deed of trust securing it, therefore, was not a purchase money mortgage. Additionally, as there was no nonjudicial foreclosure sale, antideficiency statutes were never implicated. (*Coppola v. Superior Court* (1989) 211 Cal.App.3d 848, 866 ["A 'deficiency judgment' is a personal judgment against the debtor for the difference between the debt and the proceeds received by the creditor from the sale of the security at a judicial or nonjudicial foreclosure sale"].)

B. Contractual Attorney Fees Are Recoverable as Damages If Pleaded and Proven

In 1981, the Legislature amended Civil Code section 1717 to add the following language: "Reasonable attorney's fees shall be fixed by the court, and shall be an element of the costs of suit." Reasonable attorney fees may be recovered as damages only if they are " ' "pleaded and proven—as any other item of damages—at trial." ' " (*Monster, LLC v. Superior Court* (2017) 12 Cal.App.5th 1214, 1228.) Plaintiffs did plead in the eighth, tenth, and eleventh causes of action that they were entitled to attorney fees under express provisions in the APA and the two guaranties.[15]

---

[15] The prayer for relief was inconsistent with allegations in the first amended complaint and did not seek attorney fees as damages. But "[i]t is well settled that relief may be granted in accordance with the facts alleged in a complaint and appropriate

C. Plaintiffs Were Not Entitled to "Extraordinary" Attorney Fees

This brings us to defendants' third contention, and it has merit.

Plaintiffs may have been entitled to some amount of attorney fees as damages if those attorney fees became part of the debt defendants owed under the APA, the seller note, and/or the guaranties. We say "may have been" because we also must examine the effects of the notice of default as well as whether plaintiffs' intentional failure to include the claimed fees in the recorded notice of default, acceptance of the tender in response to their payoff demand statement, and subsequent release of all liens and security estopped them from proceeding to trial on the eighth, tenth, and eleventh causes of action.

We begin our analysis with the notice of default plaintiffs recorded on February 27, 2012, several months after the seller note had been paid in full, but not yet "satisfied," and before the seller deed of trust was reconveyed. According to law firm bills received into evidence, by this date (almost one year to the day after the close of escrow), plaintiffs claimed to have incurred more than $30,000 in attorney fees. These fees were incurred primarily to protect their security on the bank loan. The balance of the claimed $81,515 in attorney fees were incurred after the notice of default.

The "extraordinary" attorney fees incurred after the notice of default may not be awarded as damages or prevailing party

---

relief will not be denied even though it be at variance with the prayer of the complaint." (*Pulos v. Pulos* (1956) 140 Cal.App.2d 913, 915.)

costs. Civil Code section 2924c regulates the attorney fees "that may be charged to a borrower . . . after notices of default and sale have been recorded. [It does] not apply to charges incurred before such notices have been recorded. . . . After the notice of default is recorded, borrowers are responsible only for the amounts stated in the notice of default plus specific costs and expenses delineated [in Civil Code section 2924c]." (*Walker v. Countrywide Home Loans, Inc.* (2002) 98 Cal.App.4th 1158, 1174 (*Walker*).) *Walker* is dispositive as to attorney fees incurred after the notice of default was recorded.

Caruso v. Great Western Savings (1991) 229 Cal.App.3d 667 is also instructive. There, the prevailing lender in a declaratory relief action was awarded attorney fees as costs. The awarded sum included attorney fees "actually incurred as an expense of the foreclosure process [after the notice of default was recorded], which fees are statutorily limited, and other fees incurred, such as those relating to the protection of the lender's deed of trust, which are not so limited." (*Id.* at pp. 676-677.) The Court of Appeal affirmed the judgment and agreed the lender was the prevailing party, but remanded so the trial court could eliminate from the prevailing party cost award those attorney fees incurred as expenses of the foreclosure process. (*Ibid.*)

As for the pre-notice of default attorney fees, Courts of Appeal have recognized that "a notice of default may include such costs as attorney fees incurred prior to the notice's recordation." (*Walker, supra,* 98 Cal.App.4th at p. 1174.) The rationale is that "[u]nder appropriate contract provisions, such expenses may be treated as collateral advances and added to the amount of the debt. Whether a particular expense may be treated as an advance, or is subject to the limitations in Civil Code section

2924c, will depend upon the purpose for which the expense was incurred *and the particular contractual terms involved*." (*Bruntz v. Alfaro* (1989) 212 Cal.App.3d 411, 421, italics added.)

Assuming, without deciding, that the APA and seller note permitted the pre-notice of default attorney fees to be added to defendants' debt under the APA and the already paid-in-full seller note, the question then becomes what, if anything, is the consequence of plaintiffs' intentionally failing to include the approximately $30,000 in attorney fees in the notice of default and in the payoff demand statement?

We begin this analysis with the language in Civil Code section 2943, subdivision (d)(3), that provides, "any sums that were due and for any reason not included in the [payoff demand statement] shall continue to be recoverable by the beneficiary as an unsecured obligation of the obligor pursuant to the terms of the note and existing provisions of law." Relying on the "for any reason" phrase, plaintiffs maintain they were entitled to intentionally omit the pre-notice of default attorney fees from the payoff demand statement, but still recover them as damages, even though the seller note was paid in full and the seller's deed of trust reconveyed. We disagree.

Plaintiffs have not cited, nor have we found, any authority that applies Civil Code section 2943, subdivision (d)(3) where the understatement was intentional, rather than the result of a mistake or error. (Compare, e.g., *Ghirardo v. Antonioli* (1996) 14 Cal.4th 39, 52 (*Ghirardo*) and *Freedom Financial Thrift & Loan v. Golden Pacific Bank* (1993) 20 Cal.App.4th 1305, 1311 (*Freedom Financial*), disapproved on another point in *Ghirardo, supra,* at p. 53, fn. 5.) This is not surprising, as Civil Code section 2943 "incorporates the common law concepts of unjust

enrichment, mistake and estoppel and provides a debtor may not receive a windfall and escape the obligation of satisfying a loan in full when a mortgage or deed of trust is retired in error. The Legislature provided [that] in these circumstances the debtor remains personally liable for the deficiency." (*Freedom Financial, supra,* at p. 1315, quoted with approval in *Ghirardo, supra,* at p. 51.)

Applying these concepts to the undisputed facts in this case, we hold plaintiffs are not entitled to attorney fees incurred before initiating the nonjudicial foreclosure, either. Defendants had no reason to suspect plaintiffs' notice of default or payoff demand statement omitted attorney fees they claimed to be owed. To the contrary, the notice of default was silent as to attorney fees and the payoff demand statement told defendants the claimed statutory attorney fees were the "actual fees due [that] can only increase by the amount of accruing interest." Any "enrichment" to defendants was not unjust. (*Ghirardo, supra,* 14 Cal.4th at p. 51 ["a party who does not know about another's mistake, and has no reason to suspect it, may not be required to give up the benefit if he also relied on it to his detriment"].)

Plaintiffs admitted they made no mistake; the decision not to pursue the additional attorney fees at the time they recorded the notice of default and presented the payoff demand statement was a calculated litigation strategy. Then, when defendants promptly paid in full, plaintiffs not only accepted the funds in complete satisfaction of defendants' obligations, they reconveyed the seller deed of trust and terminated the UCC Financing Statement. That, in turn, implicitly terminated the security agreement. As a result of these events, plus the release of the

Bouskills' guaranties, the Lehmann and Lawnland guaranties were also extinguished by their own terms.

Defendants relied on plaintiffs' representations and acted upon them. Plaintiffs' actions unambiguously told the world and defendants that the latter's obligations were paid in full and released. Under these circumstances, plaintiffs were estopped to claim additional attorney fees as damages.

Judgment for plaintiffs on the bank loan causes of action must be reversed. As a matter of law, plaintiffs cannot prevail on those causes of action. Because plaintiffs failed to dismiss them before trial, the matter must be remanded with directions to enter judgment for defendants on those causes of action.[16]

III. Prevailing Party Attorney Fees and Costs

Because we reverse the entire judgment, the trial court's award of attorney fees and costs to defendants as prevailing parties also falls.

---

[16] Having concluded plaintiffs were not entitled to attorney fees as damages, we need not address whether the trial court abused its discretion in the amount awarded.

DISPOSITION

The judgment and postjudgment order awarding plaintiffs prevailing party attorney fees and costs are reversed. Defendants are entitled to judgment in their favor on the eighth, tenth, and eleventh causes of action. Pursuant to the stipulated order, and consistent with the views expressed in this opinion, the first, second and fifth causes of action are remanded to the trial court with directions to hold a hearing or hearings on the objections, permitting the parties "to present such evidence to the Court concerning their respective objections, and any evidence in support of or in opposition thereto. The Court shall, after hearing such matters, then render its own independent determination with regard to the Accounting claims, and such determination by the Court shall be made a part of any final judgment entered in the action." Defendants are entitled to costs on appeal.

DUNNING, J.*

We concur:

BIGELOW, P. J. RUBIN, J.

---

* Judge of the Orange Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.