**No. S183523**

**First District Court of Appeal**
**Division Two**

**Case No. A125567**

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**IN THE SUPREME COURT OF THE STATE OF CALIFORNIA**

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**STEVE ROSSA and CONNIE ROSSA,**
*Plaintiffs and Respondents,*

vs.

**D.L. FALK CONSTRUCTION, INC.,**
*Defendant and Appellant.*

# REPLY BRIEF ON THE MERITS

On Appeal from the Superior Court of San Mateo County
Superior Court Case No. CIV442294
Honorable Marie Weiner

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## INTRODUCTION

The Rossas nowhere dispute that Falk was required to pay three kinds of bank charges to obtain a letter of credit as collateral for its appeal bond: (1) a letter-of-credit fee; (2) interest on sums deposited to secure the letter of credit; (3) a letter-of-credit extension fee. (Opening Brief on the Merits (OBM) 13-15.) Nor have the Rossas disputed the reasonableness of any of the charges.[1] All three were thus part of Falk's "reasonable . . . cost to procure a surety bond, including . . . the cost to obtain a letter of credit as collateral" for the bond under California Rules of Court, rule 8.278(d)(1)(F) (the "rule").

Notwithstanding the necessity and reasonableness of all three charges in procuring the letter of credit, the Rossas fervently maintain that the first charge (the letter-of-credit fee) was unquestionably a cost recoverable under the rule, but the second and third were not. But nothing in the Rossas' brief justifies the different treatment of these equally reasonable and necessary charges to obtain a letter of credit. As a matter of indisputable fact, *Falk is out of pocket for all three sums* because the Rossas induced the trial court to award an illegal and grossly excessive

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[1] Citing the declaration of Falk's employee Janice Sutton, the Rossas point out some minor discrepancies in the calculation of interest figures to suggest that the overall calculations do not accurately represent the cost Falk incurred to secure the bond. (Answer Brief on the Merits, (AB) 34, fn. 16.) In fact, the particular discrepancy cited by the Rossa is only $73.89 – a small portion of the $100,000 interest claim that was denied by the lower courts.

attorney's fee. In fairness and logic, Falk should be entitled to recover all three sums under a rule allowing it to recoup its full "cost" of obtaining letter-of-credit collateral.

Overreaching to procure an attorney's fee they were not entitled to, the Rossas effectively forced Falk to pay $100,000 to secure a debt to them it did not owe. Fundamental equity and commercial good sense – which lie at the foundation of the appellate cost rules – demand that the Rossas (and others like them) pay the fair and reasonable costs they wrongfully impose on others in the course of litigation. Because the plain language of the rule allows such an award and history, fairness, and public policy likewise support it, this Court should embrace this most beneficial construction.

## DISCUSSION

### I. INTEREST CHARGES, AS WELL AS OTHER BANK CHARGES, CAN BE A REASONABLE AND NECESSARY COST OF A LETTER OF CREDIT AS COLLATERAL FOR AN APPEAL BOND UNDER RULE 8.278(d)(1)(F).

#### A. Interest Charges Are One Part of the "Reasonable . . . Cost to Procure a Surety Bond, Including the Premium and the Cost to Obtain a Letter of Credit as Collateral" Under the Rule.

The Rossas repeatedly concede that what they call "bank fees" – a term that nowhere appears in the rule– are recoverable costs on appeal. (AB 23 ["[The Judicial Council] merely added one new particular cost, the bank fee disallowed in *Geldermann*."]; see also AB 14-16, 20-21, 25, 26, 28, 31, 44-45.) But then – inexplicably – they seek to exclude from recovery bank interest charges and loan extension fees – which are other items that likewise do not appear in those precise terms in the rule's language, but were just as much part of Falk's "cost" to procure letter-of-credit collateral for its appeal bond.[2]

All of the bank charges paid by Falk were "costs" in every meaningful sense of the term. They were out-of-pocket amounts Falk paid

[2] All rule references are to the Rules of Court. All code references are to Code of Civil Procedure unless otherwise noted.

to obtain the collateral. And they were essential to achieving that end. If Falk had failed to pay *any* of them, Falk would have had no collateral and no appeal bond.

The Rossas' interpretation of the rule is self-contradictory. While the Rossas insist that interest charges are not recoverable because that term does not appear on the face of the rule, they are just as emphatic that bank letter-of-credit fees are fully compensable – although that term is equally absent. No legal rule or principle cited by the Rossas requires magic words to describe recoverable costs on appeal. Rather, the law requires only that recoverable costs be expressed in terms that encompass a particular claimed item of expense. (OBM 22-27.)

The Rossas cite no authority for the proposition that the word "interest" – rather than a description of a category of cost items that might include interest – must always be included for interest charges to be recoverable. Similarly, there is no authority requiring the use of the term "bank fee" or "bank charge" rather than a plain-meaning description that includes those items.

A so-called strict construction of a rule need not be the narrowest one possible. And such an interpretation must still be reasonable in light of the purpose of the rule. (OBM 25-26.) Where, as here, the language of a rule authorizes broadly phrased categories of recoverable costs, the express mention of each item of cost available is not necessary to make it

recoverable. For example, the broadly-phrased catch-all provision in the trial costs statute, section 1033.5(c)(4), provides that costs neither expressly permitted nor proscribed by subdivisions (a) and (b) may nonetheless be recovered in the court's discretion. Under that authority, courts have allowed recovery of such costs as legislative histories, arbitrator's fees, and the fees of a special master, even though they are not expressly provided for on the face of the statute. (*Applegate v. St. Francis Lutheran Church* (1994) 23 Cal.App.4th 361, 364.) In complex or protracted cases, the charges of special masters and arbitrators can obviously amount to very large sums.

No authority supports the Rossas' assertion that interest may never be covered as a cost when not expressly referred to in a statute. (AB 9-10.) For example, it is well recognized that trustees may recover interest as a cost of administration although Probate Code section 15684, which governs such costs, does not expressly provide that interest is recoverable. (13 Witkin, Summary 10th (2005), Trusts, § 59, p. 633.) As in this case, it is sufficient that a recoverable cost item is within a rule's or statute's descriptive clause.

### B. The Word "Cost" Is Not Used Exclusively in Rule 8.278 to Refer to One Item of Cost.

The Rossas also insist that rule 8.278 allows for the recovery of only one cost item because the rule uses the word "cost" instead of "costs." (AB 9, 16.) From this premise, they reason that the single recoverable cost item must be the bank's letter-of-credit fee. This argument is contrary to the plain meaning of the word "cost," which can be used to describe multiple items. It also runs afoul of the rule's language in at least four ways.

*First*, the rule itself describes the "cost" to procure a surety bond as comprised of *at least two distinct kinds of costs* – the bond premium *and* the cost to obtain a letter of credit. This observation alone disposes of the Rossas' argument that the Judicial Council intended "cost" to be limited to only one item.

*Second*, the rule itself uses "cost" and "costs" interchangeably. Any distinction between the two is simply not borne out by the language.[3]

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[3] Subdivision (d)(1) reads:
(1) A party may recover only the following costs, if reasonable:
(A) Filing fees;
(B) The amount the party paid for any portion of the record, whether an original or a copy or both. The cost to copy parts of a prior record under rule 8.147(b)(2) is not recoverable unless the Court of Appeal ordered the copying;
(C) The cost to produce additional evidence on appeal;
(D) The costs to notarize, serve, mail, and file the record, briefs, and other papers;
(E) The cost to print and reproduce any brief, including any petition for rehearing or review, answer, or reply; and

*Third*, in both legal and real-world usage, "cost" carries both singular and plural meanings. "Cost" describes the amount required to obtain something. It can be ascertained from multiple sources of varying kind and amount. Black's Law Dictionary illustrates that a *cost* can include multiple components, or multiple *costs*. (Black's Law Dictionary (9th Ed. 2009) ["*Direct cost*. The amount of money for material, labor, and overhead to produce a product;" "*Distribution cost*. Any cost incurred in marketing a product or service, such as advertising, storage, and shipping;" "*Manufacturing cost*. The cost incurred in the production of goods, including direct and indirect costs."].) Thus, the cost of obtaining a letter of credit includes the bank fee for the letter of credit, any interest paid to fund it, and other expenses that may be included in the total amount required to obtain it.

*Fourth*, words like "costs" and "cost" are often used interchangeably in statutes, rules, and caselaw. California codes, including the Code of Civil Procedure, stipulate that, in statutory interpretation, the singular includes the plural and the plural the singular. (*See, e.g.*, Code Civ. Proc., § 17(a); see also Civ. Code, § 14; Bus. & Prof. Code, § 16.) This rule of construction has also been applied in California case law. (*See, e.g.*, *People*

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(F) The cost to procure a surety bond, including the premium and the cost to obtain a letter of credit as collateral, unless the trial court determines the bond was unnecessary.

*v. Catelli* (1991) 227 Cal.App.3d 1434, 1451; *Crittenden v. San Francisco Sav. Union* (1910) 157 Cal. 201, 203.)

In short, the Rossas' attempt to rest their argument on the weak reed of singular-plural distinction precipitates its immediate collapse.

**C. Nothing in the Rule's Language Precludes Interest.**

If, as the Rossas suggest, interest could not have been an intended recoverable cost, the Judicial Council could have been expected to exclude it from the broad language of the rule. It would have been easy to exclude "interest charges" or other specific items from the generally described costs made recoverable. But nothing in the rule or its history suggests any intent to exclude interest charges as part of those bank charges necessarily paid to obtain letter-of-credit collateral.

The Rossas further charge that Falk is relying on a "presumed intention" of the Judicial Council instead of the plain language of the rule. (AB 9-10.) There is no substance to the Rossas' argument. The Judicial Council demonstrated its intent by explicitly using the words "cost to obtain a letter of credit as collateral" to describe and authorize cost recovery. A bank's service fee for the letter of credit is one part of that cost; a bank's interest charge is another. If it were the Judicial Council's intention to preclude the recovery of interest, a possibility of which it certainly was aware when it enacted the 2003 amendment to the rule, then the rule's language would reflect that intent. It does not.

Finally, the Rossas misuse the maxim "*expressio unius est exclusio alterius*." (AB 9.) *Expressio unius* does not operate to exclude a cost that is *on the list* of items allowable. In this case, "cost to obtain a letter of credit as collateral" is listed, and interest is part of that cost.[4] Perhaps in response to this type of misuse, this Court and lower courts have taken significant steps toward limiting the use of *expressio unius*. "[*Expressio unius*] is no magical incantation, nor does it refer to an immutable rule. Like all such guidelines, it has many exceptions . . . ." (*Estate of Banerjee* (1978) 21 Cal.3d 527, 539 & 540, fn. 10 [listing four occasions in which the maxim is not applicable].) In a more recent case, this Court stated that it "applies only when the Legislature has intentionally changed or excluded

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[4] *Expressio unius* does not apply here for another reason: the list of two items that describe the "cost to procure a surety bond" – "the premium" and "the cost to obtain a letter of credit as collateral" – is illustrative, not exclusive. They are but two examples of the "cost to procure a surety bond," evidenced by the fact that the list is set off by the word "including." As this Court has explained, *expressio unius* is "inapplicable: . . . to a statute the language of which may fairly comprehend many different objects, some of which are mentioned merely by way of example, without excluding others of similar nature . . . ." (*Estate of Banerjee* (1978) 21 Cal.3d 527, 540, fn. 10.) Not to be misunderstood, the Court continued: "*the introductory word to the clause in controversy . . . is the word 'including.' This is not ordinarily understood as expressing an intent to limit, or to create an exception. Its dictionary meaning is: to have as part of a whole; to take into account, put in a total category, etc.*" (*Id.* at 540; emphasis added.) Therefore, it is not only true that interest is part of one of the two cost items actually listed – "the cost to obtain a letter of credit as collateral" – but it is also the case that the list itself is not even an exhaustive list of the items that could conceivably be included in the "cost to procure a surety bond."

a term by design." (*Silverbrand v. County of Los Angeles* (2009) 46 Cal.4th 106, 126.)

Moreover, California courts have been careful to observe that apparent legislative intent always trumps *expressio unius*. (*Samantha C. v. State Dept. of Developmental Services* (2010) 185 Cal.App.4th 1462, 1486, citing *In re J.W.* (2002) 29 Cal.4th 200, 209.)

No evidence of intent to exclude interest as a recoverable cost exists here, either in the rulemaking history or in the language of the rule. To the contrary, both support the Judicial Council's intent to include all reasonable and necessary charges – including bank interest charges and bank fees – incurred by a successful appellant to procure a letter of credit.

**D. As the Rossas Concede, the Only Established Legal Meaning of the Word "Cost" Is What a Successful Party Can Recover. But that Does Not Resolve the Issue of Interpretation Here.**

The Rossas argue that "cost" must be confined to its established legal meaning in decided cases. (AB 11-12.) But even they concede that there is no such meaning apart from whatever is recoverable from an opponent in litigation. As the Rossas point out: "*Here, 'cost' has a technical legal meaning – that which is recoverable after litigation.*" (AB

30, fn. 13.)[5] The Rossas do not cite any universal legal definition of "cost" that resolves the interpretive problem in this case. Nor do they cite any case or statute that provides a universally mandated definition of cost in this context. There is none. In order to determine what is recoverable, the language of the applicable cost rule must be construed.[6]

In the context of appellate costs, there is no question that a cost is something that is reasonably and necessarily paid or incurred. (OBM 48-50.) Whether a particular cost is recoverable depends on the language of the applicable appellate cost rules. Here, the applicable rule authorizes the recovery of "the cost to obtain a letter of credit as collateral" for an appeal bond. An interest charge paid by Falk is recoverable because it is a cost Falk paid to obtain letter-of-credit collateral. That is what the rule expressly makes recoverable.

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[5] All emphasis is added unless otherwise stated.

[6] The Rossas rely on an unrelated case, *Sanders v. Lawson* (2008) 164 Cal.App.4th 434, that interprets the trial cost statute, section 1033.5 and Welfare and Institutions Code section 15657.5, to assert that "cost" should be narrowly read. (AB 26-28.) *Sanders* is inapposite because it does not involve the interpretation of rule 8.278(d)(1)(F) or even similar language. The court in *Sanders* held only that Welfare and Institutions Code section 15657.5 does not cover trustee costs when only conservatorship costs are expressly allowed. In rule 8.278, however, all the costs of obtaining the letter of credit – whatever they might be – are expressly allowed.

### E. The Change in Rule 8.278 Reveals an Unmistakable Intent to Change the Law.

The Rossas argue that this Court is confined to applying the language of prior – and often unrelated – cost rules interpreted in previous cases. (AB 16-20.) Not so. The rules governing appellate costs has changed since the decisions in *Golf West* in 1986, *Sequoia Vacuum Systems* in 1964 and certainly since *Moss v. Underwriters' Report, Inc.* in 1938, all of which the Rossas cite in support of their interpretation of the current rule, which was last amended in 2007. (AB 17.)

When the Legislature or the Judicial Council amends a rule or statute, as it has done with rule 8.278, it presumably intends to change the law. (*City of Irvine v. Southern California Ass'n of Governments* (2009) 175 Cal.App.4th 506, 522; *Loew's v. Byram* (1938) 11 Cal.2d 746, 750; *People v. Weitzel* (1927) 201 Cal. 116, 118.) Even the Rossas concede that, in the 1994 amendment to the rule, the Judicial Council intended to change the law to allow what the Rossas call "bank fees" to be recoverable. The Rossas nonetheless inexplicably persist in their efforts to confine the scope of the current rule by reference to its prior versions when the Judicial Council has clearly manifested its intent to change the law.

The real question is whether the Council's undeniable intent to change the law includes rendering interest, as well as other necessary and reasonable charges to obtain a letter-of-credit collateral, recoverable as a

cost on appeal. The language chosen by the Judicial Council shows that it does.

After *Geldermann*, the Judicial Council amended the rule to allow recovery of the "other expenses reasonably necessary to procure the surety bond, such as the expense of acquiring a letter of credit required as collateral for the bond." It did not restrict its amendment to allow only the particular "bank fee" at issue in *Geldermann,* although it clearly could have done so. Instead, it chose broader language applicable to all costs to procure a letter of credit as collateral for an appeal bond. It should be taken at its word.

### F. The Legislature And The Judicial Council Are Presumed To Know The Caselaw Governing The Areas Of Law In Which They Enact Statutes And Rules.

The Rossas' discussion of rulemaking history not only misapplies inapplicable rules of construction (e.g., *expressio unius*), it disregards the ones that apply foursquare here. As this Court has held, when a statute or rule is amended, the Legislature or Judicial Council is deemed to adopt the judicial construction in effect at the time of the reenactment, unless the language of the rule expressly states otherwise. "Where a statute has been construed by judicial decision, and that construction is not altered by subsequent legislation, it must be presumed that the Legislature is aware of the judicial construction and approves of it." (*People v. Kelii* (1999) 21

Cal.4th 452, 457-458; see also *People v. Garcia* (2006) 39 Cal.4th 1070, 1087 ["When, as here, the Legislature undertakes to amend a statute which has been the subject of judicial construction, it is presumed that the Legislature was fully cognizant of such construction." (Internal quotations omitted.)

The Judicial Council adopted an amendment on January 1, 2003 that changed the language of the rule to what it currently reads and moved it to former rule 27(c)(1)(E).[7] At that time, the only judicial construction addressing interest as a recoverable cost under the immediately prior rule came from *Cooper v. Westbrook Torrey Hills* (2000) 81 Cal.App.4th 1294 (*Cooper*), *which was decided* in 2000. All prior cases – including those relied on by the Rossas – construed the language of the rule as it existed before the 1994 post-*Geldermann* amendment.

Under the established rules of construction discussed above, the 2003 amendment confirms the Judicial Council's awareness and adoption of *Cooper*'s interpretation of the rule – i.e., that interest is a recoverable cost. If the Judicial Council had disagreed with *Cooper*'s construction, it would have used the 2003 amendment to have set the matter straight. It did not do so. Instead, in light of the *Cooper* court's construction – one that included interest charges as part of the expense of letter-of-credit collateral

[7] In 2007, the rule was renumbered without language changes as rule 8.278(d)(1)(F).

– the Council retained the operative language without alteration, thereby signifying its adoption of the *Cooper* court's view.

The Rossas also contend that the Judicial Council's change of the word "expense" to "cost" in the 2003 amendment signifies a substantive change to the rule as it was interpreted by *Cooper* in 2000. (AB 22-23.) This argument is fully addressed in Falk's Opening Brief. The Judicial Council stated clearly in its Advisory Committee Comment to the 2003 amendment that any time a substantive change was intended, *including changes intended to conform older rules to current law*, it was clearly designated as such. No substantive change was identified. (OBM 32-34.)

In sum, the rule analyzed in *Cooper* in 2000 is the same in substance as the rule at issue in this case. It is *Cooper*'s construction of rule 26(c)(6) that the Judicial Council ratified when it amended the rule in 2003, thereby confirming that interest is recoverable as a cost under the rule.

## II. THE RULEMAKING HISTORY SUPPORTS THE PLAIN MEANING OF THE RULE'S LANGUAGE.

As has been detailed in previous briefing, the rulemaking history for rule 8.278(d)(1)(F), refers to the recovery, as costs, of "the expense of a letter of credit needed to secure an appeal bond." (RJN 4, quoted in OBM 31.) This language is the product of the Judicial Council's response to *Geldermann*, which involved a specific bank charge for issuing a letter of credit. But the Judicial Council did not use the words "bank fee" or "letter

of credit fee" to define the recoverable cost. Instead, it chose to amend former rule 26 to make recoverable any "other expense reasonably necessary to procure the surety bond, such as the expense of acquiring a letter of credit as collateral for the bond." (RJN 10.)

The immediately prior rule thus made fully recoverable any and all expense reasonably and necessarily incurred by an appellant to acquire a letter of credit as collateral for the appeal bond. In this case, that expense unquestionably included interest charges imposed on Falk by the bank to maintain a deposit as an express condition of issuing the letter of credit.

Oblivious to the words chosen by the Judicial Council to express its intentions, the Rossas assert that the bank "charge" referred to in *Geldermann* must be only the bank's "discrete fee" for issuing the letter of credit and no other charge, expense or cost of obtaining it. (AB 15, fn. 4 ["The use of the term 'charge' by the *Geldermann* court and the case's facts showing that only a bank fee was involved establish the limitation of Judge King's referral: interest was clearly not involved."].)

Nothing supports the Rossas' assertion. Banks charge interest as well as fees for particular services they render. Nothing in the rule's language or history distinguishes one expense or cost of obtaining a letter of credit – a bank fee for the service of issuing it – from another – the bank's interest charge on a deposit that is an express condition to obtaining the letter.

Both in law and in the world of commerce, bank "interest charges" are a fact of life. (*Abouab v. City and County of San Francisco* (2006) 141 Cal.App.4th 643, 670 [bank imposing "interest charges"]; *San Paolo U.S. Holding Co., Inc. v. 816 South Figueroa Co.* (1998) 62 Cal.App.4th 1010, 1028 [ordering "interest charges" to be paid to bank]; *Unterberger v. Red Bull North America, Inc.* (2008) 162 Cal.App.4th 414, 421 [party paid "bank charges" associated with transaction]; *Morris v. Redwood Empire Bancorp* (2005) 128 Cal.App.4th 1305, 1321 [discussing a bank's "$6 bank charge, or NSF fee, for processing each check drawn on accounts lacking funds sufficient to cover the amount of the check"].) Interest and fees are, contrary to the Rossas' suggestion, both "charges" that can be made by banks.

In a similar vein, the Rossas assert that the Judicial Council's use of the word "expense" in the singular in the rulemaking history limits its amendment to only the discrete bank fee at issue in *Geldermann*. For the same reasons discussed above, "expense" is no more necessarily singular than "cost." Indeed, the Judicial Council's rulemaking history uses the phrase "such as" to demonstrate that "the expense of acquiring a letter of credit" is only one example of a class of expenses that might be incurred to obtain a surety bond. (Rule 26, subd. (c)(6), as amended Jan. 1, 1994.)

Neither the Rossas' obfuscation of the plain language of the rule nor their misguided assault on the rulemaking history alter the manifest need to

construe this important rule as written. The same is true of the Rossas' persistent reliance on outdated caselaw that construes the very different language of prior or inapplicable cost rules. (AB 16-20.) None of the cases cited by the Rossas addresses the particular language of the post-*Geldermann* rule change. All were decided *before* the amendment at issue in this case.

## III. THE RULE SHOULD BE INTERPRETED AS BROADLY AS ITS PLAIN LANGUAGE AND HISTORY INDICATE. ITS MEANING INCLUDES INTEREST CHARGES AS ONE KIND OF BANK CHARGE MADE TO OBTAIN LETTER-OF-CREDIT COLLATERAL.

The Rossas also maintain that the broad "expense" and "such as" language originally used by the Judicial Council in the 1996 post-*Geldermann* amendment had to be scaled back because it was contrary to caselaw that refused to allow interest charges as a recoverable cost. (AB 24-25.) In doing so, the Rossas necessarily concede that interest charges can be part of the "expense" (although, they argue, not part of the "cost") of obtaining a letter of credit under the post-*Geldermann* version of the rule. If the "expense" and "such as" references did not include interest as a recoverable item, there would be no need for the Rossas to insist that the Judicial Council had to scale back the rule in 2003 by replacing "expense" with "cost" and removing the "such as" language suggesting that more than

one kind of expense was recoverable. But, as is discussed above and in Falk's Opening Brief (OBM 27-35), they are wrong about the effect of the 2003 changes. The clear history refutes their assertions.

The change that the Rossas contend took place in 2003 – which they say rendered interest charges unrecoverable as a cost on appeal – would unquestionably be a profound *substantive* change in the rule. The Rossas themselves maintain that whether or not interest is recoverable is a monumental issue with profound effects on the legal system. (AB 32-36.)

Yet the rulemaking history unequivocally states that all "substantive changes" that were part of the 2003 rule revisions were described in the Advisory Committee Comments. (OBM 32-34.) No such comment describes the removal of the "expense" and "such as" language as a substantive change. Nor does anything in the history even remotely suggest that the revision was other than stylistic. If the Judicial Council is taken at its word, the substantive change posited by the Rossas simply did not occur. Rather, the replacement of the phrase "expense reasonably necessary to procure the surety bond, such as the expense of acquiring a letter of credit required as collateral" with " reasonable . . . cost to obtain a letter of credit as collateral" was intended by the Judicial Council to have no substantive effect on recoverable cost items.

The Rossas attempt to obscure the fact that no substantive change was intended by using language from a *summary* that preceded the relevant

Judicial Council Report (RJN 78), rather than the more complete language of the report itself. (RJN 79-80, quoted in OBM 33-34.) *As the Report states, all substantive changes, including those which "conform older rules to current law" (as the Rossas contend occurred here), are reported and described in an Advisory Committee Comment. No such comment was issued for any change in the part of the rule at issue here.* Again, it follows that no substantive change occurred. (RJN 80.)

The Judicial Council's expressed intent to allow recovery of all "other expense reasonably necessary to procure the surety bond, *such as* the expense of acquiring a letter of credit as collateral for the bond" thus continues into the current language of the rule. By the Rossas' own concession, this broad "expense . . . such as" language allows the recovery of bank interest charges spent to obtain the letter of credit as one such expense. Therefore, the current rule does so as well.

Finally, the Rossas attempt to evade the Judicial Council's continuing manifestation of its intent to include interest as part of letter-of-credit expense by disregarding the relevant language in Mandatory Judicial Council Form MC-013. The form does not include a line for "bank fees." As in the pre-2003 version of the rule, the current Judicial Council Form – one that all appellants are required to use to claim their costs on appeal – requires a listing of all "other expenses reasonably necessary to procure

surety bond." (1 AA 207.) Bank fees might be one such expense. Interest charges might be another.

The Rossas insist that the Judicial Council must have been wholly unaware that the cost to obtain letter-of-credit collateral might be construed to include interest. But the Judicial Council is presumed to know the law when it amends rules. (*See, e.g., Garcia, supra*, 39 Cal.4th at 1087.) *Cooper* certainly would have alerted the Judicial Council to that prospect by its construction of rule 26(c). It was decided three years before the 2003 amendment. Additionally, *Golf West*, which was discussed in *Cooper* and on which the Rossas rely, also addressed a claim for interest included in the bank charges. (AB 18-20.)

In light of these cases, the Judicial Council would most certainly have been aware of claims that interest are a part of appellate costs. If it had intended to preclude the recovery of interest charges, it would have made clear that interest could not be recovered, or at a minimum, provided for the recovery of "bank service fees only." It did not. It allowed recovery of the full reasonable cost to obtain a letter of credit as collateral for an appeal bond, which includes necessary interest charges as well as bank service fees and charges required to procure the letter of credit.

## IV. COMMERCIAL REALITY, EQUITY, AND SOUND PUBLIC POLICY SUPPORT THE PLAIN MEANING AND HISTORY OF THE RULE.

### A. Falk's Case Demonstrates the Commercial and Equitable Factors Supporting Recovery of the Full Cost of Obtaining Letter-of-Credit Collateral.

What Falk faced in this case is a familiar scenario: An appellant is forced to obtain an appeal bond to protect its assets pending appeal. But many litigants lack the assets to post cash or to supply cash collateral for the bond. Individuals and small businesses rarely have a spare million dollars around to collateralize a bond. Instead, they must borrow money to obtain cash. The cost of borrowing is paid solely to provide security – a cash deposit in court or a letter of credit – in lieu of and for the bond. The interest charge is paid solely to protect respondent as the beneficiary of the money judgment.

Of course, when respondent is the beneficiary of a valid judgment, the bond allows respondent to recoup immediately the fruits of its judgment once the appeal is over. But when the judgment is reversed, appellant has been forced to pay for an undeserved benefit enjoyed by respondent at appellant's expense.

Simple fairness demands recompense. And that recompense should fairly include the real economic cost of the appeal – not an arbitrarily

selected small part of it because it is a "bank fee" rather than an "interest charge." The entire cost is what the rule authorizes. The entire cost should therefore be recovered.

In this case, Falk was required to make a deposit of $954,070 as security for a letter of credit. (OBM 9.) The letter of credit was necessary to collateralize an appeal bond to protect Falk from a grossly excessive attorney fee award – one that was more than six times the relatively modest $100,000 judgment obtained by the Rossas in a commercial dispute. (OBM 6, 8.) The Court of Appeal cut through the Rossas' exaggerated claims and reversed the award.[8] Falk should, in fairness, be entitled to recoup the cost of the Rossas' forensic bravado.[9]

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[8] On remand, when the correct law was applied, the result was the much smaller sum of $238,844. (Opn. 3, fn. 4.)

[9] The Rossas chide Falk's inclusion of a complete history of the parties' litigation in the Opening Brief on the merits. (OBM 3-11.) The purpose of this discussion is simply to demonstrate how easily a grossly excessive monetary award obtained through the overreaching of an unscrupulous litigant can oppress a small construction company. What happened to Falk here also happens to others. It is a cost that Falk – and similarly situated appellants – should not be forced to bear.

### B. The Rossas' Parade of Horribles Reveals No Countervailing Factor That Would Defeat Commercial Reality and Manifest Equity to Prevailing Appellants.

#### 1. Proportionality Does Not Justify Denial of Reasonable and Necessary Costs.

The Rossas complain that a decision in Falk's favor would make the costs recoverable on appeal vary from those recoverable at trial. (AB 31.) It bears repeating that trial court rules are inapposite in the determination of this case. As Falk noted in its Opening Brief (OBM 44-48), under section 1034(b), the Legislature has delegated to the Judicial Council the authority to determine recoverable appellate costs. Notwithstanding this plenary authority, the Rossas urge the Court to limit the scope of the Judicial Council's delegated power by fashioning and imposing a novel "proportionality" requirement on the recovery of appellate costs. (AB 32.)

No such proportionality rule now exists. And, with the exception of *Cooper* – a case not favorable to the Rossas – no prior decision has interpreted language that expressly allows recovery of all costs of letter-of-credit collateral for an appeal bond. This includes *Golf West*, which was decided in 1986 when rule 26(c) only allowed for recovery of the bond premium, with no mention of the cost to obtain a letter of credit.

The Rossas advocacy of a proportionality rule of uncertain parameters is impractical as well as legally unsupported. The Rossas

nowhere suggest what proportion is required.[10] Nor do they provide any reason why the restrictions that are already built in to the rule – that costs must be reasonable, necessary and out-of-pocket outlays – are inadequate to contain any excessive awards. This Court should decline the Rossas' invitation to engraft an unfathomable and unworkable exception onto the Judicial Council's lucid and sensible rule.

### 2. Employee Time, Overhead, and Opportunity Cost Are Not Out-of-Pocket Costs and Are Not Recoverable.

The Rossas maintain that allowing reimbursement of reasonable bank interest charges necessarily paid out by an appellant to obtain a letter of credit will allow recovery of "intangible and indirect expenses." (AB 33.) Not so. As Falk discussed in its Opening Brief, the requirements that costs be out-of-pocket, reasonable and necessary are already incorporated into the appellate cost rule. (OBM 48-50.) These constraints quell any speculations about future litigants' outlandish claims of employee time, overhead and the like as part of the cost to obtain a letter of credit. *Those expenses are not out-of-pocket outlays. Therefore, they are not recoverable.*

[10] Neither did the Court of Appeal. The best it came up with was a claim that "there is something like a presumption of proportionality." (Opn. 12.)

The purpose of cost statutes is "not to pay a successful litigant for his own work, but to reimburse him for his actual out-of-pocket payment for the type of costs allowed." (*Muller v. Reagh* (1959) 170 Cal.App.2d 151, 154.) The Rossas' assertions to the contrary are devoid of legal support and common sense.

### 3. Bank Charges for Interest, Like Bank Fees for Services, Are Objective, Market-based, Regulated Sums – They Are Not Subjective Opportunities to Gouge an Opponent.

The Rossas protest that the calculation of interest is so difficult that it should not be awarded. (AB 33-34.) This makes no sense. Banks charge interest in ascertainable amounts to their customers every day. Like other costs, interest charges must be actually, necessarily, and reasonably incurred. If an appellant is not required to pay such charges to obtain a letter of credit, they cannot be recovered. (OBM 48-50.)

Likewise, if an appellant pays unreasonable charges, as measured by the marketplace or regulatory limits, they cannot be allowed. If the charges are a mere accounting invention and are not actually paid or incurred, they will be denied. None of these measures is subjective. They are what courts employ every day in the exercise of their discretion to determine and award reasonable and necessary costs of litigation. (*Nelson v. Anderson* (1999) 72 Cal.App.4th 111, 132 [messenger fees properly denied when found to be

"of doubtful necessity and unreasonable on their face, when compared to the probable cost of alternatives"]; *Ladas v. California State Auto. Assn.* (1993) 19 Cal.App.4th 761, 774 [cost of meals eaten during local depositions was stricken because the expense was not necessary]; *Murphy v. F.D. Cornell Co.* (1930) 110 Cal.App. 452, 455 [cost of obtaining a description of property was stricken for failure to show necessity of the description].)

**4. Falk's Charges Were Reasonably and Necessarily Incurred.**

Given the Court of Appeal's affirmance of the trial court's ruling that interest charges were not a recoverable cost, the Rossas attack on technical aspects of Falk's interest claim is misplaced. The lower courts never resolved any such issues. In any event, the assault is vapid and misdirected.

The fee award at issue in this case was against Falk – the corporation. David L. Falk, its principal, had to supply his credit and assume personal risk to obtain the deposit for the letter of credit. The corporation reimbursed him for doing so. This is not self-dealing. Nor did it lack the indicia of an arm's-length transaction. For both Falk and David L. Falk, Wells Fargo Bank imposed the charges that had to be paid. The Rossas never alleged – let alone proved – that Falk acted unreasonably or had access to cheaper funds than it obtained through its agreement with the

Bank. If the corporation's arrangement with its principal was unreasonable, the Rossas could have proven that with reference to ordinary commercial rates and practices in the marketplace. They proved nothing. Their bogus allegations are rank speculation and conjecture and should be treated as such.[11]

### 5. The Rossas Did Not Reasonably Rely on the Language of the Rule in Obtaining a Grossly Excessive Attorney Fee Award Against Falk.

The Rossas claim that they will have been blindsided if ordered to reimburse Falk for the cost of a letter of credit. They intimate that they may not have decided to defend Falk's appeal if they were not confident of their immunity from interest charges as a cost on appeal. (AB 45-46.) But the language of the rule supports Falk's claim and renders the Rossas' reliance on prior law unreasonable. While Falk contends the rule is clear, at a minimum there is a controversy about its meaning that is worthy of this Court's attention. The Rossas could not reasonably have relied on it when they made their exorbitant attorney's fees claim.

Under established law, the Rossas' alleged reliance is unreasonable in these circumstances. (See *People v. Watson* (2008) 43 Cal.4th 652, 689

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[11] The Rossas' allegations of discrepancy in the interest claimed (AB 34, fn. 16) are likewise without merit. Moreover, even if there were discrepancies, they may justify a reduction in the court's discretion, but not the outright denial of charges as a matter of law that occurred in this case.

["Where, as here, the Supreme Court resolves a conflict between lower court decisions, there is no clear rule on which anyone could have justifiably relied to bar retroactive application."].) Moreover, it strains credulity that the Rossas – who overzealously claimed both damages and attorney fees in this case – would not have proceeded in defending the appeal if they thought they could have been charged another $100,000.

In sum, no equities favor the Rossas – or any respondent – that fails to sustain a money judgment on appeal and refuses to pay the full cost of the surety bond its conduct in litigation required. There is nothing unfair or offensive to public policy in requiring the Rossas to pay the direct cost of their own strategic choices in litigation.

## V. *COOPER* WAS CORRECTLY DECIDED AS TO BOTH OF ITS HOLDINGS.

*Cooper* was based on two independent and sound premises. First, deposits and bonds must be treated equally as demanded by section 995.730. Second, rule 26(c) included interest charges as part of the cost of letter-of-credit collateral for an appeal bond. From these two independent premises, the *Cooper* court reasoned that "the cost of obtaining a bond is recoverable, the cost of making a cash deposit is also recoverable." (*Cooper*, *supra,* 81 Cal.App.4th at 1300.) The *Cooper* court's decision is grounded in sound legal principles and logical reasoning.

The Rossas apparently question *Cooper*'s adherence to section 995.730's command to treat cash deposits and bonds equally in all contexts. But neither they nor the Court of Appeal challenged that premise. Because the two must be treated equally, there is no basis to distinguish *Cooper* from this or any other case involving the cost of letter-of-credit collateral. The only question is whether rule 26(c) was correctly construed.[12]

The Rossas claim that Falk's position is inconsistent in its analysis of *Cooper* and the statutes relied on in that case. There is no inconsistency in Falk's position. *Cooper*'s reliance on section 995.730 was proper. As *Cooper* shows, cash deposits and bonds must be treated the same by statutory command. This mandate is equally applicable in both trial and appellate contexts, so it controlled in *Cooper* as it does here.

The Rossas' reliance on section 995.250, which allows recovery of bond premium costs, is likewise misplaced. That statute embodies a cost rule that does not in any way restrict the Judicial Council's plenary authority to define and prescribe recoverable costs on appeal under section 1034(b). Moreover, nothing in the statute – which merely insures the recovery of statutory and certain other bond premiums – forecloses the recovery of interest charges or any other costs of procuring letter-of-credit

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[12] The Rossas point out that *Cooper* involved a predecessor rule. (AB 37, fn. 17.) As is shown above, no substantive change was made in the rule after *Cooper* before it was applied in this case. Falk has refuted all of Rossas' contrary suggestions.

collateral for appeal bonds. Therefore, *Cooper* was correct in declining to apply the statute.

The Rossas finally insist that this Court should abstain and defer to the Legislature to resolve this issue. (AB 43.) But they also point out that the Legislature has reserved for the Judicial Council the determination of recoverable costs on appeal. (AB 42.) The Judicial Council has spoken on this issue by the enactment of rules of court. No new law or deference to the Legislature is necessary to resolve this dispute. The law is already written. The only thing needed is this Court's interpretation of what the Council has done.

## VI. THE COURT OF APPEAL'S DECISION VIOLATES EQUAL PROTECTION.

A constitutional issue is not automatically waived if it is brought for the first time on appeal. (*Hale v. Morgan* (1978) 22 Cal.3d 388, 394.) "As a general rule, issues not raised in the trial court will not be considered on appeal. However, it is settled that a change in theory is permitted on appeal when a question of law only is presented on the facts appearing in the record." (*Blankenship v. Allstate Ins. Co.* (2007) 186 Cal.App.4th 87, 101, fn. 5 [issue brought for the first time on appeal was allegation of violation of equal protection]; see also *Phillips v. TLC Plumbing, Inc.* (2009) 172 Cal.App.4th 1133, 1141; *Duffens v. Valenti* (2008) 161 Cal.App.4th 434, 451.)

Whether the Court of Appeal's decision violates equal protection is a pure question of law involving an important question of public policy. As such, it should be addressed by this Court in its interpretation and administration of court rules.

As the Rossas correctly note, the state equal protection clause requires that similarly situated people be treated similarly. (AB 48.) Under *Cooper*, a person who deposits cash in lieu of a bond may recover interest. But under the Court of Appeal's opinion here, Falk, which obtained a surety bond, was not allowed to recover interest as a cost of procuring it. Because the Legislature has commanded that bonds and cash deposits be treated equally, the allowance of interest for deposits and the denial of interest for bonds constitute disparate treatment of similarly-situated persons.

There is no question that the Legislature has required parity between cash deposits and bonds under Section 995.730. The Legislature itself sees no rational basis to distinguish between them. In fact, there is none. The Rossas nowhere establish otherwise. They give no reason why costs should be recoverable for interest charges on a cash deposit but not a bond.[13]

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[13] There is a reason, however, for different treatment of appellants and those litigants seeking costs after a trial. The Legislature itself has so recognized by relinquishing authority over appellate costs to the Judicial Council in Section 1034(b), while maintaining total control over trial costs. In addition, appellate costs are different in kind – involving matters such as record and bonding expenses – than trial costs.

Equal protection law does not tolerate this type of unjustified disparate treatment. It should be applied here.

## CONCLUSION

The rule expressly authorizes recovery of all necessary, reasonable, out-of-pocket costs incurred to obtain letter-of-credit collateral for appeal bonds. The interest charges Falk had to pay are among the explicitly described costs. The rule already contains mechanisms to control unreasonable or outlandish cost claims. No such claims are at issue here. The requested interest charges should have been awarded to Falk under the rule.

Like many other appellants who fall victim to erroneous money judgments, Falk had to borrow money to post collateral in order to protect its assets on appeal. Denying Falk fair recompense for its interest expense – exacted because an erroneous monetary award – is not only inequitable, it unjustly rewards unsuccessful litigants and ultimately fosters illegitimate claims. This is contrary to the law and public policy of our state. It should not be endorsed by a decision of this Court.

DATED: March 2, 2011

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**CERTIFICATE OF WORD COUNT**
**(Cal. Rules of Court, rule 8.204(c)(1))**

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DATED: March 2, 2011

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Executed on March 2, 2011 at Davis, California

Rebecca N. Sells