Filed 1/20/05

CERTIFIED FOR PUBLICATION

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FIRST APPELLATE DISTRICT

DIVISION FOUR

THE STATE OF CALIFORNIA ex rel. KAMALA HARRIS, as District Attorney, etc., et al., Plaintiffs and Appellants, v. PRICEWATERHOUSECOOPERS LLP, Defendant and Appellant.	A095918 (San Francisco County Super. Ct. No. 993507)
THE STATE OF CALIFORNIA ex rel. KAMALA HARRIS, as District Attorney, etc., et al., Plaintiffs and Appellants, v. OLD REPUBLIC TITLE COMPANY et al., Defendants and Appellants.	A097793

Under the rein of Donald Barr, who personally embezzled millions of dollars while serving as chief financial officer (CFO) of Old Republic Title Company (ORTC) and related entities,[1] the management of the company initiated a variety of illegal practices. The continuation of these practices ultimately led to an action by the District Attorney and City Attorney of the City and County of San Francisco

[1] ORTC and Old Republic Title Information Concepts (ORTICON) are wholly owned subsidiaries of Old Republic Title Holding Company, which in turn is a wholly owned subsidiary of Old Republic International (ORI). For purposes of these consolidated appeals, we refer to these entities collectively as "Old Republic."

(City) against Old Republic, as well as consumer class actions. Along the way these actions were consolidated and the governmental plaintiffs also sued PricewaterhouseCoopers LLP (PwC), the accounting firm that prepared the independent audit reports for ORTC that were submitted annually to the California Department of Insurance (DOI).

This consolidated litigation splits into two branches: One follows the False Claims Act (FCA),[2] the other follows the unfair competition law (UCL).[3]

The FCA actions against Old Republic and PwC focused on the systematic failure of ORTC to honor its obligation to escheat dormant funds to the state under the unclaimed property law (UPL).[4] The government sued Old Republic for not disclosing its escheat liability in filings with the DOI and pursued PwC for allegedly submitting false audit reports that also masked this liability.

As a threshold matter the trial court ruled that the City, through its district attorney and city attorney, had standing to pursue its FCA claims as a qui tam plaintiff on behalf of the State of California. Old Republic and PwC vigorously oppose this ruling on appeal. The ruling is correct. On the merits the government prevailed against Old Republic but met defeat at the hands of PwC, failing to convince the trial court that the allegedly false audit reports were material under the FCA. In appeal No. A097793, the government and Old Republic both find fault with the trial court's measure of damages against Old Republic. Again, we conclude the trial court got it right. In appeal No. A095918, the government challenges the summary judgment in PwC's favor on its FCA claim. We conclude the trial court acted improvidently and therefore reverse.

In the UCL litigation, the trial court concluded that certain cost avoidance and arbitrage practices of ORTC generated millions of dollars in illegal interest that

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[2] Government Code section 12650 et seq.

[3] Business and Professions Code section 17200 et seq.

[4] Code of Civil Procedure section 1500 et seq.

belonged to ORTC's escrow customers. The court entered orders for restitution as well as penalties for violations related to these and other practices, and granted injunctive relief. Old Republic challenges the arbitrage ruling as well as the trial court's decision awarding interest to class plaintiffs on certain lender funds. Class plaintiffs and the People challenge rulings related to the statute of limitations and class certification, as well as the disbursement float; class plaintiffs attack the order for injunctive relief as insufficient. All of these rulings were correct. Finally, the People contest the dismissal of its UCL claim following the sustaining of PwC's demurrer without leave to amend. This claim should proceed and therefore we reverse the judgment of dismissal.

I. FACTS

A. *The Company*

ORTC is an underwritten title company licensed by the DOI to conduct business as a title and escrow agent in California. (See, e.g., Ins. Code, § 12389.) It provides title and escrow services for real estate transactions in California. As a regulated entity, ORTC has disclosure and reporting obligations to the DOI. (*Id.*, § 12389, subd. (a)(4).)

Donald Barr was ORTC's CFO from approximately 1979 until July 1996, when he was fired for embezzlement in connection with the company's cost avoidance program, discussed below. ORTC referred these allegations to the San Francisco District Attorney (SFDA). The SFDA opened a criminal investigation leading to Barr's arrest and subsequently charged him with multiple counts of grand theft, perjury, embezzlement and tax evasion. Barr negotiated a disposition in exchange for information concerning certain alleged illegal business practices of ORTC (discussed below), and pleaded guilty to two counts of tax evasion.

B. *Business Practices Subject to Litigation*

1. *Failure to Escheat Unclaimed Funds*

As escrow agent, ORTC receives funds from purchasers, sellers, borrowers and lenders; prepares documents and closing account statements; and disburses

escrow funds at the close of escrow. The company routinely aggregates its customers' escrow funds in demand deposit[5] accounts with various banks throughout California. At times, customers would fail to instruct ORTC to disburse all the funds on deposit. On other occasions a party to whom ORTC disbursed funds from the escrow account at the close of escrow would fail to cash the check. In both cases these dormant funds accumulated and remained in the accounts after the close of escrow. By the late 1980's, ORTC began sweeping some of the dormant funds from escrow accounts into its general fund and recognizing these funds as income. Under the UPL, holders of unclaimed funds such as ORTC are charged with submitting holder reports to the State Controller on an annual basis that disclose the nature, and last known owner, of the unclaimed funds. (See Code Civ. Proc., § 1530.) At the same time, the reporting holders are to deliver all escheated property identified in the reports to the State Controller. (*Id*., § 1532, subd. (a).)

At relevant times, PwC or its predecessor Coopers & Lybrand was the independent public accountant for ORTC. PwC's scope of work included preparing the annual audit report for the Commissioner of Insurance (Commissioner), as required by Insurance Code section 12389, subdivision (a)(4).[6]

Gerard Fisher, PwC's audit manager on ORTC's account during 1990, indicated he understood that ORTC had a policy of clearing dormant funds out of trust accounts. He suspected that the company had been violating the "laws related to escheat." Fisher testified that the majority of dormant funds taken from the accounts did not belong to ORTC. In 1990, PwC recommended that ORTC evaluate

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[5] A "demand deposit" is a deposit payable on demand. (12 C.F.R. § 204.2(b)(1) (2004).)

[6] Pursuant to this statute, each year underwritten title companies such as ORTC must submit to the Commissioner an audit certified by independent auditors. The purpose of this and related requirements is "to maintain the solvency of the companies subject to this section and to protect the public by preventing fraud and requiring fair dealing." (Ins. Code, § 12389, subd. (d).)

the dormant escrow amounts which remained unclaimed and review its policies to ensure compliance with state law. ORTC indicated it would do so " 'insofar as practical.' " Between 1990 and 1994, PwC raised the issue of dormant funds with the company.

Karman Pejman, a former PwC auditor, testified that there was always a concern about ORTC's practice of purging funds from escrow accounts and rerouting them to the company's operating income. He noted that ORTC's liability for funds that should have been escheated accumulated year after year. For example, for the period 1989 and 1990, nearly $1.7 million was purged from ORTC escrow accounts, with $1.3 million taken in as income. According to Pejman, ORTC never, in recent history, complied with the UPL.

Richard Baker, PwC auditor partner on the Old Republic account, was also aware of the company's dormant funds practices and knew they were recurrent.

Nonetheless, PwC issued an unqualified, "clean" audit opinion letter, which ORTC submitted to the Commissioner along with its financial statements. PwC understood that its opinion was so submitted. E. John Larsen, a certified public accountant and professor of accounting, gave his expert opinion that once PwC learned of the escheat violations, minimum auditing standards required the firm to take steps to estimate ORTC's potential liability. It did not. Without an estimate, PwC should not have issued unqualified opinion letters.

Alfred Bottalico, bureau chief of DOI's Field Examination Division (FED), explained that his division conducts field audits at company offices, whereas the Financial Analysis Division of the DOI receives and monitors the audit reports and financial statements and determines when a field examination is in order. One trigger point for a field examination would be a qualified opinion letter from an independent auditor. One of the field examination protocols is to determine if the company has its own procedure "to set up an unclaimed property liability." If fraud were detected as part of the exam, it would be a "major finding" and would spur further inquiry.

DOI undertook an examination of Old Republic and issued its confidential report in February 1999. The special examiner found that since 1980, the company had swept funds left dormant in escrow accounts into its general fund. Further, in some years Old Republic actually *budgeted* for potentially escheatable income, thus demonstrating its "systematic approach to the movement of funds into their income accounts."

ORTC did not escheat any unclaimed escrow funds to the state until 1992. The company filed its first holder report in the early 1990's. The holder reports for 1992-1994 and 1997 understated the full amount of escheatable funds which ORTC held. After the City served Old Republic with the complaint in this lawsuit, the company escheated $9,551,527.89 in unclaimed funds and $7,710,118.18 in statutory interest on those funds to the State Controller.

2. *Cost Avoidance and Arbitrage Practices*

a. *Federal Regulatory Framework*

The Federal Reserve Act[7] prohibits member banks of the Federal Reserve System from directly or indirectly paying any interest on any demand deposit. (12 U.S.C. § 371a; see also 12 C.F.R. § 217.1 et seq. (2004) (Regulation Q).) Regulation Q defines interest as "any payment to or for the account of any depositor as compensation for the use of funds constituting a deposit. A member bank's absorption of expenses incident to providing a normal banking function or its forbearance from charging a fee in connection with such a service is not considered a payment of interest." (12 C.F.R. § 217.2(d) (2004).)

From time to time the Federal Reserve Board (Board) has issued rulings and opinion letters which spell out various arrangements by which banks can provide benefits to depositors without violating the Federal Reserve Act or Regulation Q. For example, a bank can withhold or impose a reduced charge for services or benefits

[7] Act of December 23, 1913, 38 Statutes at Large 251, chapter 6; see also title 12 United States Code section 226.

reasonably regarded as normal banking functions or services, so long as the bank does not actually pay money to the demand deposit customer. Thus, under this rationale, the Board does not regard the provision of free checks, safety deposit boxes, night depository service, messenger and armored car services and the like as constituting the indirect payment of interest. (See 1957 Fed. Res. Interp. Ltr. (Jan. 23, 1957) ; 1974 Fed. Reserve Bd. Interpretive Letter, Fed. Reserve Reg. Service 2.540 (Jan. 3, 1974); 1964 Fed. Reserve Bd. Interpretive Letter, Fed. Reserve Reg. Service 2-439 (July 17, 1964).) Similarly, the Board regards automated escrow closing trust accounting and bank reconciliation, and monthly general ledger and financial statements pertaining to escrow accounting services as normal banking functions for which a bank may absorb the expenses. (1994 Fed. Reserve Bd. Interpretive Letter, Fed. Reserve Reg. Service (Apr. 26, 1994).)

Moreover, the Board has deemed that banks do not pay interest by offering loans at favorable rates for the purchase of investment instruments pledged as security for the loans to customers who maintain large demand deposit balances. In this situation, the amount of credit a bank is willing to extend is tied to the historical average demand deposit account balances. (1988 Fed. Reserve Bd. Interpretive Letter, Fed. Reserve Reg. Service 2-545.1 (June 28, 1988).)

b. *Cost Avoidance Arrangements*

ORTC provides direct escrow services in Northern California; it serves as a subescrow in Southern California. In both instances, ORTC deposits aggregated escrow trust funds in demand deposit accounts in various banks.

Starting in the early 1980's, ORTC entered into various "cost avoidance" arrangements with approximately 10 different banks which maintained the escrow accounts. Through these arrangements, a participating bank would make a certain dollar amount of "earnings" credits available to ORTC on a monthly basis. This is the way it worked: First, the bank would establish an "earnings credit rate" expressed as a percentage, and determined by reference to a market index for the bank's cost of funds. Next, it would calculate the average daily balance of funds

held in ORTC non-interest-bearing demand deposit accounts for the previous month. From that balance the bank would deduct the "float" (checks deposited which were not yet "good funds"), as well as reserves and premiums imposed by federal regulators, resulting in an average net balance. This net balance would be multiplied by the earnings credit rate, to generate the actual earnings or vendor credit.

Fees for services provided directly by the bank such as check processing, wire services and stop payments were netted out, and the net credit was multiplied by an agreed upon percentage rate, the product being the "available earnings credit." At the end of the month, the bank would pay "vendors" on invoices submitted for "normal banking services" in an amount up to the available earnings credit determined for the previous month.

Through the mid-1990's, Barr used the cost avoidance program to embezzle approximately $2 million. Barr would submit phony invoices to the banks under a shell corporation he created and controlled, and skim some of the remitted funds before transferring the remainder to ORTC.

Since July 1994, most of the earnings credit payments were paid against invoices from ORTICON. ORTC officers responsible for the ORTICON invoices never consulted with ORTICON prior to preparing them. In fact, the operations manager for ORTICON was unaware that these invoices were being submitted to banks until he was deposed in connection with this litigation. Through at least 1997, checks paid on the ORTICON invoices were deposited directly into ORTC's account.

ORTICON invoices reflected charges for computer equipment, software support and maintenance, training, escrow data accounting, and data processing. Invoices were prepared by determining the amount of available earning credits. The amount billed and entered on any given invoice generally was based on the earnings credit available at the time, not the actual cost or value of services rendered by ORTICON to ORTC. These amounts were generally slightly less than the available

earnings credit. Unused earnings credits were carried forward to the next month and ORTC would bill down to zero at the end of the year.

For the period 1987-1994, ORTC collected over $19.2 million through the cost avoidance scheme. From July 1994 through February 2001, it collected $13,760,901.

c. *Arbitrage Scheme*

Beginning around 1997, ORTC and its banking partners largely replaced the cost avoidance arrangements with an "arbitrage" scheme. The arbitrage relationship typically worked this way: ORTC would receive a rock-bottom interest loan (.25 percent to 1 percent) from the bank for an amount equal to approximately 90 percent of the total average daily balances maintained at that bank. Under agreement with the bank, ORTC was required to use the loan proceeds to purchase interest-bearing instruments from the same bank. These instruments secured the loan. ORTC retained the "arbitrage yield" or "spread" constituting the excess interest earned by the instrument over the life of the loan. For the period July 1994 through February 2001, the arbitrage yield totaled $18,377,222.

William Sarsfield, a former bank president, national bank examiner with the Office of the Comptroller of the Currency, and adjunct faculty member at Golden Gate University, testified by declaration that in his opinion "there was no business purpose for the 'arbitrage' loan other than pay net interest to Old Republic . . . on the escrow demand deposits."

3. *Fees Charged for Services Not Rendered*

ORTC also engaged in charging fees for services it did not perform. In some Southern California counties, it collected reconveyance fees from its escrow customers—typically from $65 to $75—even though neither the beneficiary nor the trustee had demanded the fee. ORTC transferred the fees to an "advance account" and paid out the fee if requested by the trustee or beneficiary. However, in many instances neither demanded a reconveyance fee and periodically ORTC would transfer the accumulated fees into company income.

After the complaint in this case was unsealed, the State Controller's Office (SCO) audited ORTC. Both parties agreed that ORTC was not able to document adequately that it was entitled to take $5,621,657 in fees into income. ORTC tendered this amount together with $1,322,844.13 in interest to the SCO. Of these amounts, $2,009,623.70 in fees and $154,727.51 in interest were attributable to fees charged on or after January 1, 1994. This translates into unearned reconveyance fees collected from approximately 80,309 customers.

In approximately 10 percent of its escrow transactions, ORTC also charged its customers $25 on average for each outgoing wire transfer. In most cases Old Republic did not actually incur the expense except insofar as the bank absorbed the fee as part of the cost avoidance and arbitrage programs.

4. *Customer Practices with Respect to Escrow Accounts*

Old Republic's written escrow instructions did not inform customers that they could place funds in an interest-bearing account. If a customer nonetheless made such a request, Old Republic honored the instruction.

Further, its form escrow instructions directed that all disbursements from the escrow account be made by check. Indeed, most disbursements were made by check rather than by wire transfer. Whereas wire transfer funds are withdrawn immediately from an account, disbursement checks take some time to clear, resulting in a disbursement float.

C. *Procedural History*

1. *The City and Class Plaintiffs Sue Old Republic*

The SFDA and San Francisco City Attorney filed the complaint[8] in this lawsuit in March 1998. They sued (1) on behalf of the City as a qui tam plaintiff under the FCA on allegations of falsifying records to conceal escheat obligations; and (2) in the name of the People on other causes of action, including a civil

[8] Pursuant to the FCA, San Francisco filed the complaint under seal. (Gov. Code, § 12652, subd. (c)(2).)

enforcement action under the UCL for (a) collecting disguised interest under cost avoidance and arbitrage schemes, but not paying the benefits to consumers per Insurance Code section 12413.5;[9] and (b) improper retention of reconveyance fees. (Collectively, we sometimes refer to these plaintiffs as the government or governmental plaintiffs.)

Barr filed his own FCA complaint in April 1998, but because the governmental plaintiffs filed first, Barr's suit has been preempted. (Gov. Code, § 12652, subd. (c)(10).) As well, several class actions were filed against Old Republic mirroring the government's action,[10] but not the FCA allegations. The trial court (1) certified a class consisting of "ALL PERSONS AND ENTITIES IN CALIFORNIA WHO, DURING THE PERIOD OF JULY 24, 1994 THROUGH FEBRUARY 7, 2001, WERE PARTIES TO ESCROWS DIRECTLY WITH OLD REPUBLIC TITLE COMPANY, WHO DID NOT RECEIVE INTEREST EARNED ON FUNDS DEPOSITED IN ESCROW"; and (2) consolidated the class and government actions for all purposes. Excluded from the class were those consumers, primarily in Southern California, who were indirectly affected by Old Republic's conduct as a subescrow.

a. *FCA Cause of Action*

Old Republic demurred without success to the FCA cause of action on grounds the governmental plaintiffs lacked standing to sue as qui tam plaintiffs, and also unsuccessfully renewed this challenge on summary adjudication. As well, the City moved for summary adjudication on this cause. Based on Barr's submission of false holder reports to the State Controller which concealed ORTC's failure to escheat dormant funds to the state, ORTC conceded liability. Accordingly, the trial

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[9] Insurance Code section 12413.5 states in part: "Any interest received on funds deposited in connection with any escrow which are deposited in a bank . . . shall be paid over by the escrow to the depositing party to the escrow . . . ."

[10] Class plaintiffs have alleged additional causes of action not germane to this appeal.

court granted the City's motion, determining that the damages were the stipulated statutory interest amount of $7,568.079, trebled to $22,704,237 and offset by interest already paid, for a net award of $15,136,158. The trial court awarded the City one-third of the trebled damages, or $7,568,079.

b. *UCL Cause of Action*

i. *Pretrial Phase*

Pretrial, Old Republic sought to exclude from any restitution award to consumers the cost avoidance and arbitrage benefits forthcoming from lender funds held in escrow, arguing that consumers have no right to them. The trial court disagreed, ruling that when a borrower is charged interest *prior to* close of escrow on funds deposited by the lender, the borrower is entitled to any interest earned on those deposits.

ii. *Trial: Liability Phase*

The matter proceeded to a bench trial on the Business and Professions Code section 17200 allegations that ORTC committed unfair, unlawful or fraudulent business practices by failing to remit to the depositing parties the benefits collected on escrow deposits under the cost avoidance and arbitrage schemes. The trial court made three significant rulings.

First, it held that although the proper interpretation of "interest" within the meaning of Insurance Code section 12413.5 is not governed by Regulation Q, there were sound reasons for construing "the California statute much like the federal provisions have been interpreted." Accordingly, the court limited the term "interest" in Insurance Code section 12413.5 to money paid for the use or deposit of money, excluding from that definition other benefits that could be given in exchange for the deposit of funds. On this point the court concluded that in determining whether a particular transaction involved interest for purposes of section 12413.5, Regulation Q and federal interpretations thereof should be looked to for guidance, but were not conclusive.

Second, the court ruled that although cost avoidance benefits sanctioned by Regulation Q do not constitute interest, the benefits paid by banks to ORTC on ORTICON invoices did because the practices in question did not comply with Regulation Q. Old Republic has not appealed this ruling.

Third, the court drew the line at equating "interest" under Insurance Code section 12413.5 with "interest" as interpreted under Regulation Q when it came to analyzing benefits conferred to Old Republic under arbitrage arrangements. Specifically, it concluded that while the Board sanctions the extension of arbitrage benefits by banking institutions for purposes of banking regulation, the extension of those benefits to ORTC are nothing but interest for purposes of Insurance Code section 12413.5: "The arbitrage benefits . . . serve no function other than to permit the payment of an ascertainable sum of money to ORTC. . . . The arbitrage arrangements are, purely and simply, means of circumventing the restrictions that apply to the payment of interest on demand deposits by doing in two steps what cannot be done in one. While permitting this practice may not undermine the objectives of the bank regulations, permitting ORTC to retain these monetary benefits—i.e., interest—cannot be squared with the explicit directive of section 12413.5." (Fn. omitted.)

iii. *Remedies Phase*

The parties stipulated that ORTC received $13,760,901 and $18,377,222, respectively, during the class period from its cost avoidance and arbitrage programs. In its decision on remedies, the trial court ordered restitution to class members of interest received by ORTC through its cost avoidance and arbitrage programs during the class period,[11] but only for amounts earned prior to close of escrow. The court

[11] The court refused to add to the stipulated totals $1,165,000 in cost avoidance benefits illegally obtained through C.E.B., Inc. (CEB)—a shell corporation created and controlled by Barr for which Barr made restitution to ORTC in 1998. The court reasoned that although the payment was made in 1998, the funds were earned *prior to* the class period.

allowed interest on the consumer float ($6,700,799) and most of the interest earned on the "lender float" ($4,853,113), but disallowed interest on the disbursement float. "Consumer float" refers to funds deposited in escrow by the buyer or refinancing party, while "lender float" refers to funds deposited in escrow by a financial institution that is lending funds to a party to the escrow. The court also awarded class plaintiffs prejudgment interest in the stipulated amount of $2,210,640. Additionally, the court imposed civil penalties of (1) $3.57 for each of the 207,324 stipulated transactions under the cost avoidance scheme, for a total of $741,850; (2) $2.55 for each of the stipulated 259,155 violations under the arbitrage scheme, for a total of $660,824; and (3) $17.50 for each of 28,709 reconveyance fee violations and $6.25 per each wire transfer fee violation, totaling $778,640.

Finally, the court ordered ORTC to (1) develop a plan for court approval for crediting the account of its escrow customers with interest earned on deposits through cost avoidance and arbitrage programs; (2) draft statements disclosing the consumer's right to have escrow funds deposited in an interest-bearing account; (3) draft disclosures concerning availability and cost of wire transfers; and (4) refrain from charging escrow customers for bank services, the costs of which are not actually incurred by ORTC. Thereafter Old Republic moved for approval of interim compliance plans, which the court approved, along with the disclosures set forth in the plans.

Subsequently, the governmental plaintiffs moved for civil penalties based on ORTC's dormant fund practices. Finding 10,000 incidents had occurred, the trial court imposed a *conditional* penalty of $173.18 per violation[12] under Business and Professions Code section 17206, for a total penalty of $1,731,800, to kick in only if we reversed the treble damages award under the FCA. With an affirmance, the penalty imposed is $1.

[12] This amount represented the average size of swept escrow accounts.

2. *The City Names PwC as a Defendant*

Meanwhile, with the fourth amended complaint filed in August 2000, the City named PwC as a defendant, asserting violations under the FCA and UCL for failure to disclose ORTC's escheat liability in audit reports filed with the DOI. PwC demurred to both causes. Sustaining the demurrer without leave to amend as to the UCL claim, the court concluded that the DOI does not have responsibility for policing escheat laws. In any event, since the funds had been returned, affected consumers could put in a claim and thus there was no additional remedy to impose.

PwC also moved for judgment on the pleadings on the FCA claim, contending that the City lacked standing to pursue the action as a qui tam plaintiff. The trial court denied the motion, declining to revisit its previous ruling. Thereafter, PwC obtained summary judgment on the FCA count. The trial court reasoned that even if PwC had disclosed the escheat irregularities, in the normal course of events and under normal procedures such information would not have been forwarded to the State Controller for enforcement action and hence the alleged misrepresentations were immaterial.

3. *Judgment and Postjudgment Matters*

The trial court entered judgment accordingly and thereafter denied motions for new trial brought by Old Republic and the class plaintiffs. Multiple appeals and cross-appeals followed. In No. A097793, Old Republic has appealed and the governmental plaintiffs and class plaintiffs have separately cross-appealed. In No. A095918, the governmental plaintiffs have appealed and PwC has cross-appealed.[13]

In August 2002, Old Republic abandoned its challenge to certain aspects of the judgment which it satisfied by paying penalties, restitution, prejudgment interest, postjudgment interest and litigation costs. In November 2002, Old Republic further

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[13] The Attorney General has filed an amicus curiae brief in support of the governmental plaintiffs. California Land Title Association has submitted its brief in support of Old Republic.

partially satisfied the conditional judgment awarding penalties under Business and Professions Code section 17206 for dormant fund practices.

II. FCA LITIGATION

A. *Threshold Issues*

In the FCA litigation, the City sued Old Republic and PwC[14] as a qui tam plaintiff. The FCA authorizes lawsuits to recover misappropriated government funds by three types of plaintiffs: (1) the Attorney General, with respect to claims involving state funds or both state and local funds (Gov. Code, § 12652, subd. (a)(1), (2)); (2) the prosecuting authority of a "political subdivision" for claims involving local funds or both local and state funds[15] (*id*., subd. (b)(2)); and (3) "a person" for claims involving state or local funds (*id*., subd. (c)). The FCA refers to the "person" bringing such an action "as the qui tam[16] plaintiff." (*Ibid*.) These actions commonly are called "whistleblower" actions.

Defendants insist that (1) the City is not a "person" within the FCA and therefore lacks standing to bring a qui tam action; and (2) the allegations upon which the FCA action is based were publicly disclosed prior to commencement of this action, thus triggering a statutory bar to jurisdiction. We disagree with both points.

1. *The City Has Standing to Bring a Qui Tam Action*

According to defendants, the plain language, legislative history, structure and purpose of the FCA all converge to support their position that the term "person" refers only to private actors.

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[14] In this section entitled "FCA Litigation," we refer to Old Republic and PwC collectively as defendants.

[15] The City does not contend that local funds are at stake.

[16] "Qui tam" is short for qui tam pro domino rege quam pro se ipso in hac parte sequitur, meaning " ' "who pursues this action on our Lord the King's behalf as well as his own." ' " (*City of Pomona v. Superior Court* (2001) 89 Cal.App.4th 793, 797, quoting *Vermont Agency of Natural Resources v. United States ex rel. Stevens* (2000) 529 U.S. 765, 768, fn. 1.)

a. *Statutory Language*

We start with the statutory language, which does not contain the word "private." Rather, it states that " '[p]erson' includes any natural person, corporation, firm, association, organization, partnership, limited liability company, business, or trust." (Gov. Code, § 12650, subd. (b)(5).) The word "includes" ordinarily is a term of enlargement, not limitation. (*Ornelas v. Randolph* (1993) 4 Cal.4th 1095, 1101.) Indeed, courts have long accepted that government entities are statutory "persons." For example, in *City of Pasadena v. Stimson* (1891) 91 Cal. 238, 248, our Supreme Court recognized a city's standing as a "person" under a provision of the Civil Code permitting "any person" to bring a condemnation action. The court reasoned that under the general provisions of the Civil Code, a corporation is a person and thus, any public or private corporation could exercise the statutory condemnation rights.

Later, in *State of California v. Marin Mun. W. Dist.* (1941) 17 Cal.2d 699, our state's high court construed section 680 of the Streets and Highways Code, providing that any "person" maintaining a pipeline could be required to move it upon written demand when necessary for safety or public improvement purposes. The issue was whether section 680 encompassed municipal water districts. Another provision of the code defined "person" as "any person, firm, partnership, association, corporation, organization, or business trust." (*State of California v. Marin Mun. W. Dist., supra*, at p. 704; see former Sts. & Hy. Code, § 19.) Explaining that the application of section 680 to municipal water districts would not limit their otherwise valid power but would only operate to prevent them from exercising their franchises in a manner contrary to law, the court concluded that the Legislature intended to embrace municipal water districts within the statute's application thereby affording a method of enforcement. (*State of California v. Marin Mun. W. Dist., supra*, at pp. 704-705.)

More recently, the court ruled that a statute precluding prescription of property of public entities by "any person, firm or corporation" was *not* limited to private parties, but rather included governmental agencies. (*City of Los Angeles v. City of*

San Fernando (1975) 14 Cal.3d 199, 276-277, disapproved on another point in *City of Barstow v. Mojave Water Agency* (2000) 23 Cal.4th 1224, 1248.)

Defendants' argument that in the absence of express words to the contrary, states and political subdivisions are not encompassed within the general words of a statute (citing *Estate of Miller* (1936) 5 Cal.2d 588, 597) misses the mark. As explained in *City of Los Angeles v. City of San Fernando, supra,* 14 Cal.3d 199, the rule *excluding* governmental agencies from the operation of general statutory provisions pertains "only if their inclusion would result in an infringement upon sovereign governmental powers. 'Where . . . no impairment of sovereign powers would result, the reason underlying this rule of construction ceases to exist and the Legislature may properly be held to have intended that the statute apply to governmental bodies even though it used general statutory language only.' [Citations.]" (*Id.* at pp. 276-277.)

Not surprisingly, defendants argue that if local governments were "persons" under the FCA, they would also be subject to liability thereunder. FCA liability, in turn, would infringe on their sovereignty by interfering with provision of public services.[17] This argument was put to rest in *LeVine v. Weis* (1998) 68 Cal.App.4th 758. There, a school district contended it was not a "person" within the FCA and thus could not be sued for wrongful termination under the employee whistleblower provisions of the act. The reviewing court held that the definition of "person" must be read in light of the context and purpose of the statute—namely, to protect the public fisc. Thus a broad interpretation should be given to the person or entity allegedly raiding the public treasury and there was no reason to deny protection when

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[17] Apparently, the City has contended in another case that imposition of liability under the federal FCA would infringe on its governmental obligations. (See brief of amici curiae City of New York, City of Los Angeles, City and County of San Francisco, and Cook County, Illinois at p. 23, in *Vermont Agency of Natural Resources v. United States ex rel. Stevens, supra,* 529 U.S. 765 [1999 WL 651614] [concerning federal FCA].) The California FCA is patterned on a similar federal act. (*Laraway v. Sutro & Co.* (2002) 96 Cal.App.4th 266, 274.)

the raider was a governmental entity. So construed, the definition of person was broad enough to encompass the school district within the terms "association" and "organization." (*Id*. at pp. 764-765.) The court dispatched the sovereign powers argument with these words: "[N]o governmental agency has the power, sovereign or otherwise, knowingly to present a false claim. The very notion is repugnant to how government should operate by and for the people. [The district] is subject to the False Claims Act." (*Id*. at p. 765.)

Defendants are also adamant that including public entities within the definition of "person" for purpose of qui tam standing is not sound public policy. For example, PwC casts the City's prosecution of this lawsuit as opportunistic, arguing that the qui tam provisions are designed to provide financial incentives for whistleblowers, and that the FCA reflects an effort to " 'walk a fine line between encouraging whistle-blowing and discouraging opportunistic behavior.' " (Quoting *U.S. ex rel. Springfield Terminal Ry. v. Quinn* (D.C. Cir. 1994) 14 F.3d 645, 651.) Surely the prosecution of this action by public officials poses substantially less risk of being parasitic than actions by purely private actors. Moreover, depriving public entities standing would disserve the remedial purposes of the act. A liberal construction of the term "person" encourages competent prosecution of false claims by public qui tam plaintiffs for the public good.

Defendants attempt to modify "persons" with "private" by hearkening the doctrines that (1) words are known by the company they keep;[18] and (2) the meaning of each item in a list should be determined by reference to the others, with preference given to an interpretation that uniformly treats items similar in scope and nature.[19] They argue that the entities identified as "persons" do not include any governmental bodies and thus "person" should be interpreted narrowly as embracing only private actors. We disagree. The catalog of actors randomly contains some specific terms

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[18] See *Heller v. Norcal Mutual Ins. Co*. (1994) 8 Cal.4th 30, 49-50.

[19] See *Kelly v. Methodist Hospital of So. California* (2000) 22 Cal.4th 1108, 1121.

associated with private parties—namely "natural person," "partnership" and "business," but other specific terms such as "trust" can be public (charitable) or private, as can a corporation. Finally, the terms "association" and "organization" are general enough to embrace either. Thus, these doctrines do not aid defendants.

b. *Structure of the FCA*

Defendants also maintain that the structure of the FCA supports their interpretation, relying on the rule that the statutory expression of some things necessarily means other things not expressed are excluded. (See *Lake v. Reed* (1997) 16 Cal.4th 448, 466.) They reason that since the FCA allows for actions by the Attorney General and qui tam plaintiffs and expressly and separately allows for actions by political subdivisions but only to recover local funds, the Legislature has implicitly accorded political subdivisions a limited place in the statutory scheme that forecloses standing in other instances, namely when local funds are not involved. We are more persuaded by the City's argument that rather than reflecting an intent to exclude municipalities from suing as qui tam plaintiffs, in light of the FCA's broad remedial purpose, the Legislature meant to enlarge the universe of remedies available to municipalities. Suits prosecuted by the prosecuting authority of a political subdivision are available when local funds are at stake, *in addition to* suits that municipalities and other public entities can bring as a "person," whether or not local funds are involved. Nor does this interpretation render the separate provision for political subdivision suits superfluous. That provision is necessary to make it clear that when a political subdivision acts as prosecuting authority in cases involving its *own* funds, it need not follow procedures required of qui tam plaintiffs, namely submitting the suit to the Attorney General for review. (Gov. Code, § 12652, subd. (c)(3).) Additionally, a political subdivision can *intervene* in actions brought by the Attorney General involving local funds. (*Id*., § 12652, subd. (a)(2), (3).)

Defendants attempt to bolster their position by alluding to certain procedural requirements for qui tam complaints "filed by a private person." (Gov. Code,

§ 12652, subd. (c)(2).)[20] But of course the prior subdivision, which creates the qui tam right of action, does not contain the "private" qualifier. (*Id.*, § 12652, subd. (c)(1).) "Where the Legislature has employed a term or phrase in one place and excluded it in another, it should not be implied where excluded." (*Phillips v. San Luis Obispo County Dept. etc. Regulation* (1986) 183 Cal.App.3d 372, 379.) Nor must we infer an intent to restrict qui tam actions to private persons in order to "harmonize" the two subdivisions. While the reference to "private" person in Government Code section 12652, subdivision (c)(2) may detract from the statute's precision, it does not cancel out the broader meaning, nor does it compel the conclusion that the Legislature intended to single out political subdivisions for a less favored status than private individuals or entities.

c. *Legislative History*

Defendants also champion the legislative history of the FCA as supporting a narrow reading of the term "person." First, they point out that the original version of Assembly Bill No. 1441 (1987-1988 Reg. Sess.) as introduced on March 4, 1987, enumerated various governmental entities in the definition of "person." That version also provided only for civil actions brought by the Attorney General or by "any person" on behalf of the person and the people of the State of California. Thereafter, the specific enumeration of governmental entities was removed from the definition of "person." Concurrently, a new definition for "political subdivision" and a new right of intervention and action by the prosecuting authority of a political subdivision with respect to local funds was created.

Defendants point us to *Wilson v. City of Laguna Beach* (1992) 6 Cal.App.4th 543, 555, holding that an enactment should not be interpreted to include a provision

[20] This provision reads: "A complaint filed by a private person under this subdivision shall be filed in superior court in camera and may remain under seal for up to 60 days. No service shall be made on the defendant until after the complaint is unsealed."

contained in the bill as originally introduced, but later rejected. They draw an overly simplistic conclusion from this general proposition.

Here, the proposed amendment eliminating language from the definition of "person" simultaneously created a definition and distinct action for political subdivisions. The Legislative Counsel's Digest for the original bill simply stated that the bill "would authorize the Attorney General and any other person to bring a civil action for the people of the state." (Assem. Bill No. 1441, introduced Mar. 4, 1987 (1987-1988 Reg. Sess.) p. 1.) The digest to the proposed amendment, and each digest thereafter including the digest to the chaptered bill, advised the legislators: "The bill would authorize the Attorney General, the prosecuting authority of a political subdivision and any other person to bring a civil action for the people of the state or of the political subdivision . . . ." (Legis. Counsel's Dig., Assem. Bill No. 1441 (1987-1988 Reg. Sess.) 4 Stats. 1987, Summary Dig., p. 523.) There is no reference to "private" persons in any of the Legislative Counsel's Digests for Assembly Bill No. 1441.

Courts frequently rely on the Legislative Counsel's Digest to discern evidence of legislative intent. (See *Rockwell v. Superior Court* (1976) 18 Cal.3d 420, 443; *People v. Tanner* (1979) 24 Cal.3d 514, 520; *Maben v. Superior Court* (1967) 255 Cal.App.2d 708, 713.) Indeed, it is reasonable to presume the Legislature adopted an act with the intent and meaning expressed in the Legislative Counsel's Digest. (*Maben v. Superior Court*, *supra*, at p. 713.) We conclude from this slice of legislative history that rather than demonstrating an intent to deprive political subdivisions of standing as qui tam plaintiffs, this history suggests the Legislature contemplated a broad definition of "person" in the role of qui tam plaintiff, one which gave all plaintiffs standing to redress harm to either state or political subdivisions. While the Legislature probably did not anticipate that political subdivisions would be typical qui tam plaintiffs, neither does the history suggest it intended to *eliminate* them as potential qui tam plaintiffs. In light of the inclusive

language of the definition of person and the statute's remedial purpose, we find defendants' reading of the legislative history unduly narrow.

Defendants also call our attention to several references tying qui tam plaintiffs to "private" persons or parties scattered in a few legislative committee reports and an analysis of Assembly Bill No. 1441 prepared by the public interest organization that proposed the legislation. These references are not convincing. We are persuaded that the definition of "person," broadly interpreted in a manner that supports the beneficial goals of the statute, in a manner consistent with prior Supreme Court interpretations of the term "person" and with the Legislative Counsel Digests for Assembly Bill No. 1441, includes municipalities and other political subdivisions.

Finally, defendants refer us to comments in a committee report to the effect that enactment of the FCA would not result in any increased government personnel costs or bureaucracy. They maintain this could only be true if "person" meant "private" actor. But of course the FCA contemplates that the Attorney General and local prosecuting authorities will pursue false claims on their own behalf; when they do, without doubt public resources will be redirected to those efforts.

2. *There Was No Public Disclosure*

Beyond requiring standing as a statutory person, the FCA further limits a court's jurisdiction over such claims, as follows: "No court shall have jurisdiction over an action under this article based upon the public disclosure of allegations or transactions in a criminal, civil, or administrative hearing, in an investigation, report, hearing, or audit conducted by or at the request of the Senate, Assembly, auditor, or governing body of a political subdivision, or by the news media, unless the action is brought by the Attorney General or the prosecuting authority of a political subdivision, or the person bringing the action is an original source[21] of the

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21 The FCA defines "original source" as "an individual who has direct and independent knowledge of the information on which the allegations are based, who voluntarily provided the information to the state or political subdivision before filing an action based on that information, and whose information provided the basis or catalyst for

information." (Gov. Code, § 12652, subd. (d)(3)(A).) The purpose of the public disclosure bar is to eliminate parasitic suits by persons who merely echo allegations already in the public domain and play no role in exposing the fraud in the first instance. (See *U.S. ex rel. Findley v. FPC-Boron Employees' Club* (D.C. Cir. 1997) 105 F.3d 675, 678, 688 [discussing virtually identical federal counterpart].)

Here, Donald Barr disclosed information to the SFDA about ORTC's escheat practices as part of the negotiated disposition of the charges pending against him. The disclosures were made during confidential interviews. Barr waived the right to a preliminary hearing and, as a condition of providing the information, the SFDA guaranteed confidentiality until the negotiated disposition was reached. The criminal information filed against Barr, as well as his plea agreement (which was sealed) are devoid of factual allegations which gave rise to the qui tam suit against Old Republic.

Defendants take the position that the disclosures were "publicly" made during a "criminal hearing" within the meaning of Government Code section 12651, subdivision (d). We disagree.

Although the Third Circuit has held that "disclosure of discovery material to a party who is not under any court imposed limitation as to its use is a public disclosure under the [federal] FCA" (*U.S. ex rel. Stinson v. Prudential Ins.* (3d Cir. 1991) 944 F.2d 1149, 1158, fn. omitted), other courts have rejected that view, for good reason. "[T]he reasoning of the Third Circuit is unsound. The interpretation of 'public disclosure' adopted there runs contrary to the plain meaning of the words. . . . [¶] . . . [T]he language of the statute itself is 'public disclosure,' not 'potentially accessible to the public.' A plain and ordinary meaning of 'public' is 'open to general observation, sight, or cognition, . . . manifest, not concealed' [citation]." (*U.S. v. Bank of Farmington* (7th Cir. 1999) 166 F.3d 853, 860; see also *U.S. ex rel.*

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the investigation, hearing, audit, or report that led to the public disclosure as described in subparagraph (A)." (Gov. Code, § 12652, subd. (d)(3)(B).)

Ramseyer v. Century Healthcare Corp. (10th Cir. 1996) 90 F.3d 1514, 1519 [" ' public disclosure' signifies more than the mere theoretical or potential availability of information . . . . [I]n order to be publicly disclosed, the allegations or transactions upon which a *qui tam* suit is based must have been made known to the public through some affirmative act of disclosure"]; *U.S. ex rel. I.B.E.W. v. G.E. Chen Const., Inc.* (N.D.Cal. 1997) 954 F.Supp. 195, 198 ["public disclosure require[s] actual rather than merely theoretical disclosure"].)

California adheres to the "plain meaning" rule. We concur that "public" disclosure requires an *affirmative act* of disclosure.

Defendants also contend that the relevant information was publicly disclosed because Barr divulged Old Republic's secrets to a competent official authorized to act for the public. Defendants cite *U.S. v. Bank of Farmington, supra,* 166 F.3d 853, but fail to emphasize the key point. There, the court held: "Disclosure of information to a competent public official about an alleged false claim against the government we hold to be public disclosure . . . [citation] *when the disclosure is made to one who has managerial responsibility for the very claims being made*. . . . [¶] . . . [¶] Disclosure to officials with less direct responsibility might still be public disclosure if the disclosure is public in the commonsense meaning of the term as 'open' or 'manifest' to all." (*U.S. v. Bank of Farmington, supra,* 166 F.3d at p. 861, italics added.) The SFDA is not the public entity that has any direct managerial responsibility over the escheat provisions at issue here. Rather, the State Controller is responsible for administering and enforcing the UPL. (See Code Civ. Proc., §§ 1540-1542, 1560-1567, 1571-1572, 1580.) That the SFDA and city attorney are empowered to seek penalties for unlawful acts under Business and Professions Code section 17200 et seq. does not give them "direct responsibility" for the claims at hand.

Defendants further complain that availing public prosecutors of the financial inducements afforded to qui tam plaintiffs generally creates a "dangerous conflict." As they see it, a public prosecutor could use his or her criminal investigatory powers

to obtain information and then "parasitically" file a claim based on that information. Further, rewarding a district attorney with bounty for exposing false claims takes away incentives for whistleblowers to come forward, and could implicate the due process rights of persons allegedly perpetrating fraud.

We fail to perceive the conflicts or other evils that defendants see. First, public prosecutors routinely cut deals with defendants for information implicating a wider web of wrongdoers. Here, in the course of the criminal investigation of Donald Barr, former Old Republic insider, the SFDA obtained information concerning significant illegal practices engaged in by the company. Barr pleaded guilty to two counts of tax fraud and thereafter the City filed suit against Old Republic under the FCA. What is the evil in permitting the City to reap the "bounty" as opposed to Barr, a convicted felon? In any event, Barr was not dissuaded from blowing the whistle. He filed his own qui tam complaint, three months after the City filed its complaint. Being the source of the information, nothing prevented him from filing it earlier, and beating the City to the courthouse.

Second, there is no conflict as was the case in *Tumey v. Ohio* (1927) 273 U.S. 510, cited by PwC. There, a village court was set up to try persons accused of violating the Prohibition Act. Fines received from conviction were divided between the state and village and thus the court made money for the village. The mayor tried the cases, set the fines (within a minimum-maximum range) and received a fee, but only upon a conviction. The high court did not hesitate to rule that the defendant's due process rights had been violated. Not only was the mayor personally and financially interested in the outcome of the case, but, as executive head of the village, he had an interest in and responsibility for its financial condition. (*Id*. at pp. 520, 523.) There are no such conflicts here.

B. *The Trial Court Correctly Determined the Measure of Damages Against Old Republic*

1. *Trial Court Events*

Once the FCA standing issues were resolved in the trial court, Old Republic conceded liability based on Donald Barr's submission of false holder reports to the State Controller which concealed the company's failure to deliver unclaimed funds to the state. Under the FCA, a defendant who knowingly makes or uses a false record "to conceal, avoid or decrease an obligation to pay or transmit money . . . to the state" (Gov. Code, § 12651, subd. (a)(7)) is liable for "not more than three times the amount of damages which the state . . . sustains because of" that malfeasance (*id.*, § 12651, subd. (b)).

Thereafter, the City moved for summary adjudication, arguing that the measure of damages was treble the understated escheat obligation plus the mandatory 12 percent interest required under the UPL.[22] (Code Civ. Proc., § 1577.) Old Republic asserted that since the unclaimed funds do not belong to the state but are merely held for the rightful owners, the state did not sustain any damages. The trial court took a different path, holding that the state's damage was the loss of use of the under-escheated funds during the time they were wrongfully withheld. Additionally, finding the UPL to be " 'complete within itself,' " the court ruled that the 12 percent statutory interest prescribed by Code of Civil Procedure section 1577 was the legislatively determined compensation for the loss of use of the funds. In other words, *actual* loss of use damages need not be factually determined. Both sides criticize this ruling, but we conclude it is sound.

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[22] Specifically, Code of Civil Procedure section 1577 provides: "In addition to any damages, penalties, or fines for which a person may be liable under other provisions of law, any person who fails to report or pay or deliver unclaimed property within the time prescribed . . . shall pay to the State Controller interest at the rate of 12 percent per annum" on the property or value thereof from the date the property should have been reported, paid or delivered.

2. *Legal Framework*

The UPL has dual purposes: (1) to protect owners of unclaimed property by locating them and restoring their property to them; and (2) to afford the state, rather than the holder, the benefit of using the property. (*Douglas Aircraft Co. v. Cranston* (1962) 58 Cal.2d 462, 463; see *Cory v. Public Utilities Com*. (1983) 33 Cal.3d 522, 528.) Property received by the state pursuant to the UPL does not permanently escheat to the state. (Code Civ. Proc., § 1501.5, subd. (a).) Rather, the state assumes custody of the property (*id*., § 1560, subd. (a)); sells and otherwise disposes of it as appropriate (*id*., §§ 1563, 1565) and deposits all funds received under the UPL, including proceeds from the sale of property, into the " 'Abandoned Property' " account of the unclaimed property fund (*id*., § 1564, subd. (a)).

All money in that account is "continuously appropriated to the Controller, without regard to fiscal years, for expenditure in accordance with law in carrying out and enforcing" the UPL, including the payment of claims, appraisals, and the like. (Code Civ. Proc., § 1564, subd. (b).) An appropriation " 'without regard to fiscal years' " is "available for encumbrance from year to year until expended." (Gov. Code § 16304.) Thus, the state has an obligation, continuing in perpetuity, to pay owner claims, regardless of whether at any given time the unclaimed property fund is sufficiently funded. (Code Civ. Proc., §§ 1540, 1501.5.) Notwithstanding this obligation, on at least a monthly basis the State Controller must transfer all money in excess of $50,000 to the state's general fund. (*Id*., § 1564, subd. (c).) At this point these are unrestricted stated funds: "The General Fund consists of money received into the treasury and not required by law to be credited to any other fund." (Gov. Code, § 16300.)

3. *The Damage to the State is Loss of Use, Not the Principal Amount*

The City and the Attorney General (as amicus curiae) argue that the principal of the underreported unclaimed funds is the damages which should be trebled because once these funds find their way into the general fund, the state can spend them like any other revenue source. According to this view, the loss to the state is

the unclaimed funds that should have been reported and delivered to the state but were not. In sum, they contend that damages under the FCA is the *amount of the false claim* or, in this case, the "reverse" false claim.

This argument does not hold sway. Initially, we repeat that Old Republic has already paid the under-escheated amount plus interest to the state. More importantly, although from a tracing and accounting point of view the bulk of unclaimed funds and proceeds of unclaimed property are transferred to the general fund, the state remains responsible for valid owner claims in perpetuity. There is no permanent escheat and thus the UPL can never be regarded as a scheme whose purpose it is to augment the state's capital assets.

Further, rather than dictating the measure of damages, the liability provision of the FCA simply provides that a person who commits a proscribed act is liable to the state for treble the amount of damage the state sustains because of the act. (Gov. Code, § 12651, subd. (a).) Given the State's continuing obligation to possible claimants and the absence of permanent escheat, plus the statutory purposes of the UPL, we conclude that the act of reporting and transmitting less than is required thereunder implicates the state's interest in the *use* of funds until reclaimed by their rightful owners, not the remitted funds themselves. By design, as between the state and a holder such as Old Republic, the UPL allocates the benefit of the use of unclaimed funds to the state. (*Douglas Aircraft Co. v. Cranston, supra*, 58 Cal.2d at p. 463; *Bank of America v. Cory* (1985) 164 Cal.App.3d 66, 74.) This purpose is reiterated in the legislative history of Assembly Bill No. 3815, which added and amended provisions of the UPL. (See Sen. Com. on Judiciary, Rep. on Assem. Bill No. 3815 (1987-1988 Reg. Sess.) as amended Mar. 24, 1988, p. 2.; Sen. Rules Com., Off. of Sen. Floor Analyses, 3d reading analysis of Assem. Bill No. 3815 (1987-1988 Reg. Sess.) as amended Mar. 24, 1988, p. 2.) Further, as reflected in the analysis of the Senate Rules Committee, by shortening the escheat period as proposed in the amendments, the likelihood of reuniting owners with their property would increase to

between 35 and 40 percent, in contrast to approximately 25 percent under the then-current system. (*Id*. at pp. 2-3.)

4. *Code of Civil Procedure Section 1577 Interest is the Proper Measure of Damages for Loss of Use*

Old Republic, on the other hand, is adamant that under the FCA, loss of use damages should be measured by the actual market rates in effect at the relevant times. We disagree.

Code of Civil Procedure section 1577 sets interest at 12 percent for the failure to report, pay or deliver unclaimed property within the prescribed time, commencing from that prescribed time.[23] In a case such as this, payment of the statutory interest is mandatory. Contrary to Old Republic's contention, this is not a penalty; rather, it is *in addition to* any penalties, damages or fines for which a person may be liable. (*Id.,* § 1577.) The 12 percent rate is the earnings the Legislature has determined the state should earn on late-escheated property, calculated on the amount of such property as of the date the holder should have reported or transmitted the same to the State Controller. In other words, this is the rate the Legislature has deemed adequate to compensate the state for loss of use of unclaimed property that holders fail to escheat under the UPL. (See *Bank of America v. Cory*, *supra*, 164 Cal.App.3d at p. 81 ["[t]he Controller and owners of the funds escheatable . . . can only be adequately compensated for their loss of use by the award of [section 1577] prejudgment interest"].) Since the Legislature has declared a statutory rate of interest as compensation for loss of use, the decision is removed from the hands of the litigants and the courts. Accordingly, the trial court correctly ruled that damages under the FCA for loss of use is the Code of Civil Procedure section 1577 interest, trebled, minus a set off for interest already paid.

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[23] The 2003 amendment excuses interest where the failure to report, pay or deliver is due to reasonable cause. (Stats. 2003, ch. 304, § 5.)

C. *The Trial Court Improvidently Granted Summary Judgment in PwC's Favor on the FCA Cause of Action*

1. *The Trial Court Ruling*

For purposes of this appeal, we assume that PwC submitted false reports to the government when it issued unqualified audit reports on Old Republic's financial statements for annual submission to the DOI. Although disturbed about the gravity of the alleged false submissions, the trial court concluded that full disclosure of Old Republic's escheat violations *to the DOI* would not have had a tendency to influence *the SCO*, the public entity in charge of enforcing California's escheat laws. Instead, the court found that any omissions from the audit reports were not material because the DOI would not have forwarded the information to the SCO for enforcement. The City is convinced this decision is wrong; so are we.

2. *The Materiality Standard for FCA Action*

Under the FCA, a person who knowingly submits a false report to the state or a political subdivision in order to conceal, avoid or decrease an obligation to that entity is liable for treble the damages that the entity sustained "because of the act." (Gov. Code, § 12651, subd. (a)(7).) Thus, the false claim must be material in order to qualify for FCA action.

"Materiality, a mixed question of law and fact, depends on ' "whether the false statement has a natural tendency to influence agency action or is capable of influencing agency action." ' " (*City of Pomona v. Superior Court, supra,* 89 Cal.App.4th at p. 802, quoting *U.S. ex rel. Berge v. Trustees of Univ. of Ala.* (4th Cir. 1997) 104 F.3d 1453, 1459.)[24] Reviewing precedent concerning the concept of materiality embodied in a variety of federal statutes, the high court in *Kungys v. United States* (1988) 485 U.S. 759, 771 explained: "It has never been the test of

[24] Because California's FCA is very similar to the federal act, it is appropriate to consider federal precedents in interpreting our act. (*City of Pomona v. Superior Court, supra,* 89 Cal.App.4th at pp. 801-802.)

materiality that the misrepresentation or concealment would *more likely than not* have produced an erroneous decision, or even that it would *more likely than not* have triggered an investigation. . . . [T]he central object of the inquiry [is] whether the misrepresentation or concealment was predictably capable of affecting, *i.e.*, had a natural tendency to affect, the official decision."

Under this objective standard, the focus is on the "intrinsic capability" of the false claim or report to influence or affect the governmental entity. Assessing "intrinsic capability," the court's job is to "consider whether a statement could, under some set of foreseeable circumstances, significantly affect an action by a [governmental] department or agency." (*U.S. v. Facchini* (9th Cir. 1989) 874 F.2d 638, 643 [construing 18 U.S.C. § 1001].)

3. *Factual Showing*

a. *DOI Operations and Practice*

In part I.B.1, *ante*, we outlined evidence showing the magnitude of Old Republic's escheat fraud, PwC's knowledge that Old Republic was violating the escheat laws and inflating its earnings, and the auditor's issuance of clean audit opinion letters for submission to the DOI despite this knowledge. Marshalling facts to defeat the issue of materiality, PwC proffered evidence that in the past DOI analysts and field examiners *did not* communicate with the SCO, and had not done so in years;[25] there was no documentary evidence that the DOI had cooperated with the State Controller in an investigation or referred a UPL matter to the State Controller; nor was there documentary evidence that the DOI itself had initiated disciplinary action based on the UPL or taken an enforcement interest in the UPL.

Additionally, David Lee, a supervisor in the DOI's Financial Analysis Division (FAD), testified that independent audit reports are reviewed for the purpose

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[25] Charles DePalma, supervising insurance examiner with the Field Examination Division (FED), testified that the FED used to have a working relationship with the SCO, and he personally met with representatives from the SCO about an insurer, but that was maybe 20 to 25 years ago.

of assuring the company's financial solvency. If an analyst spotted a financial problem, he or she would bring it to Lee's attention. Although no escheat violation had ever been brought to his attention, if a FAD analyst "caught" one of a magnitude that would affect the financial viability of a company, the FAD analyst would notify him and his department would follow up. For example, FAD would probably write a letter to the company to ascertain what it intended to do about the problem. Lee also explained that he would receive a copy of the final report prepared by the FED after conducting a field examination. If the report confirmed a potential problem, FAD and FED would "probably jointly work . . . to find out what the company is gonna do about the problem that they have."

Lee stated that he never conducted or requested an examination of an underwritten title company such as ORTC on the basis of failure to comply with the UPL. The discovery process in this litigation uncovered several independent auditor statements submitted since 1990 that noted the respective companies were not fulfilling their obligations under the UCL. However, these matters had not been brought to Lee's attention and he was not aware of any action taken by FAD with respect to the auditors' notes.

The FED has a set of field examination protocols which, among other things, direct the examiners to pay attention to a company's handling of escheatable funds, and call for reviewing and determining procedures for escheatable funds and stale dated checks, as well as reviewing escheat listings and regulatory filings. FED supervisor DePalma explained that when the field audit procedures reveal a company is not in compliance with escheat laws, the examiner will disclose this fact in the examination report. The examiner might also suggest to the company that it change its procedures. However, examiners do not have the authority to order a company to change procedures, or to impose a penalty or institute an enforcement action if it does not. DePalma speculated that "[m]aybe we should have a procedural report

directly to the State Controller, but we don't."[26] FED does not routinely contact SCO, but "[w]e would hope that our legal department did when they followed up on the report." If the report shows "a lot of compliance issues," DePalma would direct that "Legal" get a copy of it.

Bottalico testified that a qualified audit opinion letter would "certainly" be a "trigger point[]" that could prompt a request for a field audit. Further, detection of fraud in the course of a field examination would be a major finding that would prompt an investigation into whether management was involved, and at what level.

Bottalico supervised a 1993 periodic field examination of a title insurance company (not an underwritten title company),[27] in which the report indicated that a review of the insurer's procedures relating to uncashed checks showed that numerous checks were outstanding for a considerable time. It further noted the company in question had written procedures to appropriately identify such checks to ensure compliance with escheat laws. Bottalico stated that beyond a comment in a report, further procedures or recommendations might be warranted if, for example, the company were taking uncashed checks back into income. If the outcome were material, FED would set up a liability on the company's financial statements for those uncashed checks.

b. *Action in the Old Republic Matter*

In the fall of 1998, after the City's complaint in this case was unsealed, the SCO undertook a UPL audit of ORTC. In 1999, the DOI commenced action relating to UPL compliance in connection with ORTC. Darrel Woo, custodian of records for

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[26] Alfred Bottalico, a bureau chief with FED, stated he believed there was a time—probably in the late 1980's and early 1990's—when field examination reports were referred to the SCO as a follow-up measure when the report recommended that the company subject to examination establish an UPL procedure. He probably learned about this practice at an FED management meeting or discussions with management.

[27] FED typically examines title insurance companies every three years. Underwritten title companies are examined when a specific issue arises that needs to be addressed.

the DOI, stated that the DOI action "was taken as part of a larger investigation and at the behest of another agency."

Not only did the DOI investigate, it also took enforcement action against Old Republic. The special examiner for DOI issued a report in February 1999 which related, among other matters, that the SCO estimated the company's total escheat obligations, with interest and penalties, could reach $19 to $20 million. The report, which treated the panoply of ORTC's suspect practices, also noted that the company recently paid $10 million to the SCO. Responding to the report, the Commissioner issued a notice of hearing regarding a cease and desist order, again addressing the panoply of Old Republic's practices, including willful failure to escheat "several millions of dollars" to the state. The notice stated that the Commissioner "has reasonable cause to believe that [ORTC] is in a hazardous condition and is conducting its business and affairs in a manner which is hazardous to its policyholders, creditors and the public."[28] The notice identified three areas of illegal

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[28] PwC has objected to the notice as well as the examination report because the government submitted this evidence the day before the summary judgment hearing. It further claims that the "facts" set forth in these documents *do not exist* for purposes of appeal because they were not noted in the separate statement, citing *United Community Church v. Garcin* (1991) 231 Cal.App.3d 327, 337. This absolute prohibition against considering evidence not referenced in the separate statement has been soundly rejected because it ignores the *discretion* of the trial court to deny a motion for summary judgment for failure to comply with Code of Civil Procedure section 437(c), subdivision (b). (*San Diego Watercrafts, Inc. v. Wells Fargo Bank* (2002) 102 Cal.App.4th 308, 315.) Moreover, what *United Community Church* also explains, and PwC fails to acknowledge, is that the purpose of the separate statement requirement is to inform the court *and the opposing party* of all the facts upon which the moving party bases its motion. This is a due process protection *for the opposing party*. Further, it is clear from the record that PwC did *not* object to the late submission of these documents at the hearing, and that the court considered *all* the papers submitted. (Code Civ. Proc., § 437c, subd. (c) [referring to all papers submitted and calling on court to "consider all of the evidence set forth in the papers, except that to which objections have been made and sustained by the court"].) We defer to the trial court's implied exercise of its discretion to review late submitted papers. (See *Hobson v. Raychem Corp*. (1999) 73 Cal.App.4th 614, 625, disapproved on another point in *Colmenares v. Braemar Country Club, Inc.*

conduct, including "willful failure to escheat several millions of dollars to the State of California in violation of California Code of Civil Procedure Section 1511." The notice warned that if the Commissioner found against Old Republic, the Commissioner would order that the company "immediately cease and desist from engaging in any acts, practices or transactions" which endangered policyholders, creditors or the public.

c. *Impact of Escheat Violations on Old Republic's Solvency*

Opposing PwC's summary judgment motion, the government submitted, among other things, an evidentiary stipulation entered in the City's action against Old Republic. Pursuant thereto, the parties agreed for purposes of trial that it was undisputed ORTC had tendered $9,551,527.89 in dormant funds and $7,710,118.18 in statutory interest in satisfaction of the SCO's unclaimed property audit of the company, with a credit. The company was credited with $513,637.13 in previously escheated amounts and $966,524.10 in interest on those payments, and for a $10 million payment in December 1998. Broken down, the figures show that by December 1989, Old Republic owed the state nearly $7 million in dormant escrow funds and millions more dollars in interest. Through 1997, with continuing violation of the escheat laws, the debt mushroomed to almost $17 million, including interest. As noted above, by 1999 the SCO had estimated that total escheat liability could reach $19 to $20 million. In terms of PwC's work for ORTC, for the fiscal year 1993 audit, PwC's strategy work papers indicated that income statement materiality was estimated at $750,000 and balance sheet materiality at $4.2 million. With respect to the income figure, the PwC partner on the ORTC audit engagement testified that if the aggregation of all adjustments was "close or greater than

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(2003) 29 Cal.4th 1019, 1031 & fn. 6.) Finally, the documents do not raise theories or any new category of facts that were not already before the court as part of the government's response to PwC's separate statement.

$750,000, then we would . . . consider whether that had a material impact on the financial statements."

PwC is adamant that the stipulation referenced above is not competent evidence, arguing that a stipulation is not binding against someone not a party to the stipulation. The question is not one of the binding power of the stipulation. Certainly PwC could offer opposing evidence. Rather, the question is whether the court could consider the evidentiary stipulation on the question of the amount of Old Republic's escheat indebtedness to the state. Certainly the lower court, as well as this court, could take judicial notice of the evidentiary stipulation as a record of a court of this state relevant to the current dispute. (Evid. Code, § 452, subd. (d)(1).) PwC did not object on this basis. Moreover, its assertion that the *evidentiary* stipulation is not evidence is absurd. Evidence includes "writings . . . presented to the senses that are offered to prove the existence or nonexistence of a fact." (*Id*., § 140.) Here, the City offered the stipulation to prove the extent of Old Republic's escheat liability. The evidence is what it is—an agreement in related litigation between a party to the instant litigation and the client of the other party to this litigation that the amounts disclosed were undisputed for that particular lawsuit.

4. *Analysis*

In this reverse false claim scenario, our job is to determine whether auditor statements which disclosed management's inflation of earnings by millions of dollars based on systematic violation of the UPL would have had a natural tendency to influence —or the intrinsic capability to significantly affect—agency action. Without question the SCO is the primary enforcer of our escheat laws, and without question such disclosures would not, in the natural course of DOI business, be relayed to that office. Also without question, in the past no insurer or underwritten title company had ever been denied a license or subjected to disciplinary or investigative action or examination for failure to comply with the UPL. However, notwithstanding PwC's arguments to the contrary, although DOI is not the primary UPL enforcer, it *does* have statutory authority and practices and procedures for

enforcing laws, including the escheat laws, that impact insurance companies. Moreover, with the wheels of its internal procedures and practices humming properly, disclosure of Old Republic's escheat violations would have a natural tendency to influence DOI action.

Underwritten title companies are required to furnish an annual audit prepared in accordance with generally accepted auditing standards by an independent certified public accountant or independent licensed public accountant. (Ins. Code, § 12389, subd. (a)(4)(B).) The purpose of this and other provisions governing the conduct of underwritten title companies . . . is "to maintain the solvency of [underwritten title] companies and to protect the public by preventing fraud and requiring fair dealing." (*Id*., § 12389, subd. (d).) In carrying out these purposes, the DOI can enact reasonable rules and regulations to govern the conduct of these companies. (*Ibid*.) Further, whenever it appears necessary, the Commissioner shall "examine the business and affairs of [underwritten title companies]." (*Id*., § 12389, subd. (c).) The Commissioner also has stop order and corrective and remedial powers which the Commissioner can exercise upon a reasonable cause to believe and a determination after public hearing, that a company subject to examination is "in a hazardous condition, or is conducting its business and affairs in a manner which is hazardous to its policyholders, creditors or the public . . . ." (*Id.*, § 1065.1.) If a company violates or fails to comply with a stop order, the commissioner can exact monetary penalties and commence proceedings to revoke or suspend its license. (*Id.*, § 1065.5, subds. (a), (b).)

The DOI's FAD reviews the audit reports of underwritten title companies to evaluate their financial solvency. If an audit report revealed escheat violations that affected a company's financial viability, FAD would follow up. A qualified audit opinion letter would also be a trigger point that might prompt referral to the FED for a field audit. Field audit procedures include protocols for reviewing a company's escheat practices. In the past, examination reports have identified UPL compliance issues. Follow-up recommendations might include setting up a liability on the

company's books if the company were realizing material income from stale checks. If the examination report raised significant compliance issues, the legal Department would receive a copy of the report and if fraud were uncovered, further investigation would ensue.

Here, the People introduced evidence on the magnitude of Old Republic's escheat liability and the corresponding inflation of the company's earnings, and PwC's knowledge of the same. By PwC's own audit guideposts, the debt exceeded the cutoff for income statement materiality in 1993, many times over. Moreover, when the true facts were made known, the DOI *did* take investigative and enforcement action against Old Republic, in part because of its sizable escheat obligation to the state. True, it was not the catalyst, but the DOI did act. PwC urges that we ignore DOI's enforcement action, arguing that consideration of it would be "bootstrapping." This is not bootstrapping. PwC has trumpeted the SCO's escheat enforcement powers. This evidence shows that DOI also has such powers, although it is not the primary enforcer. The evidence also contributes to a reasonable inference that earlier discovery of the true facts concerning the magnitude of the escheat violations would have a natural tendency to influence, or would be capable of influencing, DOI action.

The trial court and PwC focused almost exclusively on the actual historical practices, procedures and outcomes within the DOI and the actions of individual government analysts and examiners. But the purpose of the FCA is "to supplement governmental efforts to identify and prosecute fraudulent claims made against state and local governmental entities." (*Rothschild v. Tyco Internat. (US), Inc.* (2000) 83 Cal.App.4th 488, 494.) Thus, our focus is primarily on the intrinsic qualities of the statements themselves and the extant structures and authority that would support ferreting out the financial wrongdoing and taking action to stop it. With this lens we conclude that the totality of evidence submitted in opposition to the summary judgment motion, from the audit requirement and purpose, to DOI's statutory and regulatory powers, to its internal procedures, to the magnitude of the escheat

violation and DOI's ultimate action, defeated summary judgment in PwC's favor. PwC did not overcome the materiality element of the FCA cause of action and therefore was not entitled to judgment as a matter of law. (Code Civ. Proc., § 437c, subd. (c).)

III. UCL LITIGATION

A. *Old Republic's Issues on Appeal*

1. *Trial Court Correctly Ruled that Arbitrage Benefits Are Interest*

The UCL authorizes civil penalties for acts of unfair competition, defined as "any unlawful, unfair or fraudulent business act or practice . . . ." (Bus. & Prof. Code, §§ 17200, 17206.) The trial court determined that ORTC committed "unlawful" acts within the meaning of the UCL because the company earned and unlawfully retained interest through its cost avoidance and arbitrage arrangements, in violation of Insurance Code section 12413.5. That law mandates that any interest received on escrow deposits shall be paid to the depositing party to the escrow unless that party instructs otherwise. Old Republic challenges this decision with respect to the arbitrage practices only.

a. *Arbitrage Benefits Are Interest within the Meaning of Insurance Code Section 12413.5*

Insurance Code section 12413.5 dictates that consumers have the superior right to any interest received on their escrow fund deposits. (*Hirsch v. Bank of America* (2003) 107 Cal.App.4th 708, 718.) Although the statute does not define "interest," from the statutory context we discern that interest is an amount "received on funds" and "paid over" "to the depositing party to the escrow" rather than being transferred to the account of the underwritten title company. (Ins. Code, § 12413.5.) Our Civil Code defines interest as "the compensation allowed by law or fixed by the parties for the use, or forbearance, or detention of money." (Civ. Code, § 1915.) As well, courts have described interest as "a *premium paid* for the use of money usually

recognized as a percentage"[29] and as " 'a *consideration paid* for the use of money or for the forbearance in demanding it when due.' "[30] From these definitions, and consistent with common usage, we agree with the trial court that although other forms of compensation or benefits *could* be extended in exchange for the use of money, "interest" as used in Insurance Code section 12413.5 refers to money paid for the use, forbearance or retention of money. As the trial court pointed out, if a bank gives a depositor a 10-pound turkey to those maintaining balances of $10,000 and a 20-pound turkey to those with $20,000 balances, a turkey may be the equivalent of interest but it is not "interest" as we know it.

In the final analysis, the spread that ORTC receives under the arbitrage arrangements is interest accruing on escrow deposits maintained with various banking institutions. It is the premium, compensation fixed by the parties, or consideration paid to ORTC by the banks for maintaining deposits with the banks.

The "low" interest loans that banks extend are not loans in any usual sense of the term. First, the interest rate is nominal. Second, the amount of the loan is tied to the historic escrow account balances on deposit. Third, ORTC cannot use the proceeds for its own business purposes. Rather, the sole purpose of the "loan" is to generate the interest differential between the reduced interest on the "loan" and the interest received on the purchased instruments, which differential is credited to ORTC's account. Thus, the company must purchase interest-bearing instruments from or through the bank, and pledge them as security for the "loan." As the trial court explained, under this scheme a direct payment of interest to ORTC is converted into a two-step process with no purpose other than producing an ascertainable amount of interest for ORTC on its escrow account balances. Although there may be a theoretical risk to ORTC in terms of repaying the loans, in reality the transactions

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[29] *Kenney v. Los Feliz Investment Co., Ltd*. (1932) 121 Cal.App. 378, 385, italics added.

[30] *Sampson v. Century Indemnity Co.* (1937) 8 Cal.2d 476, 480-481, italics added.

are risk-free. Indeed, as reflected in a verified annual report to the Commissioner, ORTC did not consider the loans to be of substance.

Old Republic argues that the differential cannot be interest within the meaning of Insurance Code section 12413.5 because the differential is paid by a third party, not the bank, on an investment, not on deposited funds. Nor surprisingly, Old Republic sticks to a literal, highly technical argument as it must. Stripped to its core substance, the interest differential is directly tied to the escrow account balances because the rock-bottom "loan" is based on that amount, and the bank is the engine that generates and funnels interest to ORTC through the third party device of investment instruments. When the instrument matures, the banks shave off their .25 to 1 percent and the arbitrage yield, being the balance remaining, is credited to ORTC. Throughout this whole process, the escrow deposits are available to the banks for their use. Thus, in essence the arbitrage yield is compensation paid by the bank to ORTC for the use of the escrow deposits. In the end, ORTC receives monetary interest from the bank on its escrow deposits.

b. *Legislative History Does Not Aid Old Republic*

Old Republic also urges that the legislative history of Insurance Code section 12413.5 and Financial Code section 854.1 assists its cause. Not so.

A 1963 proposed amendment to the predecessor of Insurance Code section 12413.5 provided that escrow holders, with the consent of the depositing party, could earn interest or income for the escrow holder's benefit for up to 60 days. (Stats. 1963, ch. 1895, § 1, p. 3887.) The enacted version, substantively identical to the relevant language of Insurance Code section 12413.5, dropped any language pertaining to investment income and eliminated the right to retain any interest on deposits. This scant history provides no clue as to any intent of the Legislature with respect to the complex arbitrage programs at issue here. Nothing in the record discloses that such programs were even a glimmer in the eyes of financial institutions at the time.

Old Republic also attempts to line up support from Financial Code section 854.1 and its legislative history, which it asserts attests to the Legislature's endorsement that arbitrage programs are permissible competitive benefits and not interest. That statute *permits* real estate brokers *functioning as mortgage loan servicers* to keep for their own account any "benefits" accruing from placement of impound funds in non-interest-bearing accounts.[31] In contrast, Business and Professions Code section 10145 *prohibits* real estate brokers from keeping interest earned on funds deposited in trust *in connection with any real estate transaction*. (Bus. & Prof. Code, § 10145, subds. (a)(1), (d)(5).)

Section 854 of the Financial Code, California's version of Regulation Q, generally prohibits banks from paying interest on demand deposits, either directly or indirectly. With the enactment of Financial Code section 854.1, the Legislature recognized a distinction between interest and benefits not in the nature of interest that may accrue from the deposit of funds. As the report of the Assembly Committee on Finance and Insurance explained, "as a class, non-interest-bearing accounts are attractive to lenders, and lenders will often woo them from depositors able to establish such large accounts, by the provision of cut-rate banking services or favorable terms on other borrowing by the depositor." (Assem. Com. on Fin. and Ins., Rep. on Assem. Bill No. 1042 (1989-1990 Reg. Sess.) as amended May 17, 1989, p. 3.)

Old Republic makes the leap that by enacting Financial Code section 854.1, the Legislature explicitly determined that benefits accruing from arbitrage programs are competitive benefits which banks can extend to demand deposit customers, and therefore such benefits are not interest. Nothing in Financial Code section 854.1 or

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[31] Reporting on the proposed legislation, the Assembly Committee on Finance and Insurance Report of June 1989 highlighted the distinction between *servicing* a real estate loan, the subject of Financial Code section 854.1, and holding funds pending a sale. As explained, funds received for loan servicing are assignable to principal and interest (belonging to the lender), taxes and insurance.

its legislative history references arbitrage programs, let alone the particular schemes in place in this case. Offering loans on favorable terms is quite different from an arrangement that dictates the purchase of commercial paper with the loan proceeds—the amount of which is tied to the escrow funds on deposit—in order to generate and credit the interest spread to an underwritten title company. With a conventional loan offered at a reduced interest rate, the proceeds are available to the borrower for business purposes and, as the trial court pointed out, the interest that is saved is "an inherently uncertain amount that is not 'paid' to the recipient."

The uncodified portion of Financial Code section 854.1[32] does not change our mind. According to the report of the Senate Committee on Banking and Commerce, the California Land Title Association had registered concern about "benefits" extended "to title companies" for demand deposits. (Sen. Com. on Banking and Commerce, Analysis of Assem. Bill No. 1042 (1989-1990 Reg. Sess.) as amended July 6, 1989, p. 2.) The senate amendments added the uncodified provision. In *Hannon v. Western Title Ins. Co*. (1989) 211 Cal.App.3d 1122, 1128 (*Hannon)*, the court held that absent a contrary instruction, an escrow holder has no duty to deposit funds in an interest-bearing account. Further, an escrow holder is not a trustee within the meaning of Probate Code section 16004, and does not have the powers or duties of a true trustee. (*Hannon, supra*, at p. 1129.) In this regard, the plaintiff in *Hannon* had alleged that the title insurance company breached its fiduciary duty by receiving " 'interest, gratuities and other benefits' " from the depository bank in exchange for the deposit of escrow funds in a non-interest-bearing account. (*Ibid*.) *Hannon* cannot be read as approving arbitrage programs or any other particular practices of title insurance, controlled escrow or underwritten title companies; nor can Financial Code section 845.1.

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[32] "Nothing in this act shall affect the permissibility of any deposit relationship or practice that is not expressly covered by Section 854.1 of the Financial Code nor abrogate or modify in any manner the holdings of Hannon v. Western Title Insurance Company, 89 D.A.R. 8451." (Stats. 1989, ch. 305, § 2, pp. 1388-1389.)

c. *Regulation Q Does Not Govern Interpretation of Insurance Code Section 12413.5*

Old Republic further contends that we should construe "interest" as it is used in Insurance Code section 12413.5 in complete harmony with Regulation Q, as interpreted by federal regulators, and that California regulators consistently have followed the federal definition. We disagree, for several reasons.

As mentioned earlier, the Board has issued an interpretive letter determining that arbitrage arrangements essentially identical to those engaged in by Old Republic and its banking partners do not violate Regulation Q. (1988 Fed. Reserve Bd. Interpretive Letter, Fed. Reserve Reg. Service 2-545-1 (June 28, 1988) [LEXIS 150].) However, nothing in the language of Insurance Code section 12413.5 or the statutory scheme to which it belongs[33] suggests that the Legislature intended to incorporate Regulation Q into section 12413.5.

Indeed, the general counsel of the Federal Reserve Bank of San Francisco has acknowledged that Regulation Q *does not* control the interpretation of Insurance Code section 12413.5. "I understand that state law requires that any interest paid on an escrow account be paid over to the ultimate beneficiary, and not retained by the escrow company. The Federal Reserve's positions on what is and is not a payment of interest *are only for Regulation Q purposes, and should not be regarded as in any way determinative of whether an escrow company's retention of the benefits provided by a bank as compensation for an escrow deposit is appropriate under state law*." (June 16, 1995 letter from Robert Mulford, Vice-President and General Counsel, Federal Reserve Bank of San Francisco, to the Legal Analyst of the Department of Insurance, p. 3, italics added.)

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[33] Insurance Code section 12413.5 comes within article 6 (Rebates and Commissions) of chapter 1 (Title Insurance) of part 6 (Insurance Covering Land) of the Insurance Code.

Old Republic cites to the deposition testimony of a Hon Chan, an employee of the DOI, asserting that state regulators "turned first" to the Board on the issue of whether there was a violation of Insurance Code section 12413.5. However, Chan was unequivocal that Regulation Q and Federal Reserve opinions were not determinative, but were looked to as guidance and "an additional source of information."[34]

Moreover, no regulations or guidelines have been promulgated by a California administrative agency concerning the receipt of earnings credits or cost avoidance and arbitrage benefits, the applicability of Regulation Q to California law on the subject of interest, or the like. Although there is some reference in the record to the understanding of a top official in California Land Title Association that the Commissioner had committed to adopting such guidelines, no guidelines were ever drafted.

Old Republic also holds up a March 3, 1998 letter from the chief of the Enforcement Division of the DOI stating: "[T]he Department finds no per se prohibitions in the Insurance Code against [arbitrage] practice[s]. Nevertheless, the Department believes that it is the title company's obligation to carefully analyze the facts and circumstances of each particular arrangement to ensure that the title company does not violate its fiduciary duties as escrow holder and trustee of the escrow funds, and does not violate any other applicable laws."

This letter, in the nature of an informal opinion, lacks analysis and is not persuasive. The persuasive power of an agency's interpretation of a statute is circumstantial and depends on the presence or absence of factors supporting the merit of the interpretation. (*Yamaha Corp. of America v. State Bd. of Equalization* (1998)

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[34] Old Republic also contends that California's "banking regulators" have consistently followed the lead of Regulation Q rulings in deciding whether state chartered banks pay interest on demand deposits, a practice forbidden by Financial Code section 854. The letter to which Old Republic refers *condemns* a particular scheme as violative of Regulation Q.

19 Cal.4th 1, 12.) These include "indications of careful consideration by senior agency officials" (*id*. at p. 13), evidence that the agency has consistently maintained the particular interpretation, and "indications that the agency's interpretation was contemporaneous with legislative enactment of the statute being interpreted" (*ibid.*). The letter in question fails all these criterion. Moreover, we are more deferential when faced with a quasi-legislative administrative decision. Informal, ministerial actions do not merit the same deference; nor does an agency's interpretation of a statute, as opposed to *its own* regulation. (*Id*. at pp. 7, 12.) Finally, while finding no blanket prohibition against arbitrage, the letter itself cautions scrutiny of the details of a particular arrangement, which the lower court undertook.

d. *The Trial Court's Reasoning Was Sound*

Old Republic also assails the trial court's stated reasons for its arbitrage ruling, complaining that they have nothing to do with the concept of interest. The company first attacks the court's finding that the low-interest loans are not real loans because the company must purchase treasury bills or other investment instruments with the proceeds and pledge them as security. Old Republic argues that restrictive loan terms and collateral requirements are normal banking practices, not components of interest. Old Republic misses the court's point, namely that the "loans," which were tied directly to the sum of escrow deposits, were an artifice that allowed Old Republic to receive a specified interest differential for its own account.

Further, Old Republic takes umbrage with the court's assessment that ORTC did not bear any real risk that the return on its purchase of commercial paper would be insufficient to repay the rock bottom "loans" extended by the banks. Old Republic's contention is that risk is an unworkable standard and unrelated to any operative concept of interest. This argument goes nowhere. Old Republic inserted the issue into the proceeding, arguing that it was "taking the risk and making the investment with its own money," not with the escrow deposits. The court merely deflated Old Republic's risk analysis as a justification for its interpretation of "interest."

Finally, Old Republic criticizes the court's conclusion that the arbitrage program has no "independent function" and serves no purpose other than facilitating the payment to ORTC of a sum certain of money. Relying on FRB interpretive letters, Old Republic reasons that the foregoing of charges (that is, market rate interest) is not interest. Again, these interpretations do not control. As important, the trial court made its arbitrage ruling in consideration of the whole package—not just the rock-bottom interest.

In any event, the trial court's fundamental interpretation of interest within the meaning of Insurance Code section 12413.5 is sound. To exclude the arbitrage spread as a component of interest depletes economic substance from the term, exalts form over any notion of substance, and encourages implementation of disguised, purposefully nontransparent transactions, to the detriment of the consumer. Indeed, the purpose of section 12413.5 is to *protect* the escrow customer. The statute makes it abundantly clear that absent escrow instructions to the contrary, *any* interest received on a customer's escrow deposits belongs to them, and is not to be transferred to the account of the title company. Given the expansive and protective nature of the provision, we interpret it to mean *any* interest, whether directly or indirectly earned on escrow funds.

e. *Old Republic's Federal Preemption Argument Fails*

Old Republic maintains that the trial court's arbitrage ruling interferes with and frustrates federal banking law, and thus federal law preempts Insurance Code section 12413.5, as interpreted. (See *Grimes v. Hoschler* (1974) 12 Cal.3d 305, 310 [state statute is preempted if it "interferes with and frustrates a federal statute" or " ' "stands as an obstacle to the accomplishment and execution of the full purposes and objectives" ' " of federal law].)

Old Republic did not raise this issue in the trial court, and thus it is waived. (*Pool v. City of Oakland* (1986) 42 Cal.3d 1051, 1065-1066.)

On the substantive front, Old Republic has not made a cogent statement of the federal banking law purpose it believes is thwarted by a rule that arbitrage benefits

must be passed through to California escrow depositors as interest. Old Republic says that if the trial court's interpretation prevailed, title and escrow companies would have no incentive to participate in arbitrage programs and thus, state law in effect would "prohibit" a federally approved banking practice. But surely the purpose of Regulation Q, as interpreted to permit arbitrage programs, is not merely to maintain the existence of that practice.

In any event, the trial court's interpretation does not thwart the practice. Insurance Code Section 12413.5 provides that interest on escrow funds must be paid to the depositing party "unless the escrow is otherwise instructed by the depositing party . . . ." Any title company is free to draft escrow instructions that, with full disclosure to and agreement from the depositing party, direct that the arbitrage interest differential be paid to the company. It is a matter of disclosing the pertinent costs and benefits to the customer.

Old Republic also suggests that arbitrage practices have been approved to enable federal banks to compete for substantial demand deposit customers. The interpretive letters it cites are highly technical and do not state such a purpose. Even if such a purpose could be inferred, Insurance Code section 12413.5 as interpreted by the trial court does not thwart it. The statute applies across the board to interest received on escrow funds on deposits in *any* institution, whether a federal or state bank, a savings and loan association, or an industrial loan company. Federal banks are not rendered noncompetitive by this ruling because *all* financial institutions are impacted uniformly with respect to escrow deposits, as are *all* title insurance, underwritten title and controlled escrow companies in California. Nor would federal banks gain a competitive edge from a contrary ruling because again, *any* financial institution could compete for escrow deposits by offering arbitrage benefits for the account of such companies, without regard to Insurance Code section 12413.5. Further, notwithstanding the trial court's interpretation, companies would still have an economic incentive to seek out such benefits for their customers as a competitive tool vis-à-vis companies that do not negotiate arbitrage benefits for their customers,

and because they could charge for the service. The effect postulated by Old Republic is attenuated at best and too insignificant to implicate federal preemption. (*Peatros v. Bank of America* (2000) 22 Cal.4th 147, 158 [stating that any conflict must be " 'of substance and not merely trivial or insubstantial' "].)

Finally, the general counsel of the Federal Reserve Bank of San Francisco has opined that Regulation Q has no preemptive effect over state law concerning the payment of interest on escrow deposits. To reiterate, in his June 1995 opinion letter, the general counsel indicated that the Federal Reserve's determinations of what is interest for purposes of Regulation Q "should not be regarded as in any way determinitive [*sic*] of whether an escrow company's retention of the benefits provided by a bank as compensation for an escrow deposit is appropriate under state law."

f. *Later Stipulated Judgments Have No Collateral Estoppel Effect*

Old Republic further urges that the People should be "collaterally estopped" from *relitigating* the arbitrage issue on the basis of stipulated judgments against *other* companies entered *after* judgment was rendered in this case. Each stipulated judgment defines "financial benefit" this way: "The term 'financial benefit' means any consideration, other than consideration denominated as interest, that defendants obtain from a financial institution in connection with the defendants' deposit of escrow funds with that financial institution. 'Financial benefit' includes a financial institution's absorption of expenses incident to providing normal banking functions or its forbearance from charging a fee in connection with providing normal banking functions or services, including those normal banking functions and services that the Federal Reserve Board determines may be provided without full charge consistent with 12 C.F.R. part 217. Examples of 'financial benefits' . . . include, but are not limited to, escrow accounting services and bank reconciliation, wire transfers, and loans at preferential interest rates." Old Republic asserts that these judgments "are a powerful and persuasive statement by the California Attorney General that banking benefits that are not interest under federal law also are *not* interest under § 12413.5."

First, the stipulated judgments have no preclusive effect because they did not exist when judgment was entered in this case. The doctrine of collateral estoppel, while nuanced and complex in some respects, is straightforward with respect to sequencing: It bars *subsequent relitigation* of issues actually litigated and determined in a prior action involving one or more of the same parties. (See *Todhunter v. Smith* (1934) 219 Cal. 690, 695; see also *Bernhard v. Bank of America* (1942) 19 Cal.2d 807, 811-813; *Estate of Gump* (1991) 1 Cal.App.4th 582, 608.)

Second, the stipulated judgments never define interest, they define "financial benefits" which term excludes "consideration denominated interest." And, although they refer to low-cost loans, they do not refer to arbitrage programs. Third, the judgments direct that the full value of any "financial benefits" be allocated to the company's escrow division and used exclusively to underwrite the cost of escrow services. In other words, the benefits inure to the customer, not the escrow holder!

g. *Cases from Other Jurisdictions Are of No Help*

Finally, Old Republic posits that "[e]very other court that has considered the question has ruled cost avoidance and arbitrage benefits are not interest." This is an overstatement, to say the least. While the cases discuss benefits under cost avoidance and earnings credits arrangements, they do not address the arbitrage schemes at issue here, let alone Insurance Code section 12413.5. The sine qua non of an arbitrage scheme is to consistently yield a sum certain interest differential for the benefit of the title insurance, controlled escrow or underwritten company based on, and in consideration of, the substantial escrow funds on deposit during the applicable time. On the other hand, the absorption of costs for specific bank-related functions and services yield benefits received in nonmonetary form and serves some independent function. Hence, this out-of-state authority does not advance our deliberations.

For example, the court in *Washington Legal Found. v. Legal Found. of Wa* (9th Cir. 2001) 271 F.3d 835 (en banc), affirmed *sub nom. Brown v. Legal Foundation of Wash.* (2003) 538 U.S. 216 generally discussed earnings credits used

to offset bank fees for services and charges such as accounting services and wire transfers, and distinguished such benefits from interest, but said nothing about arbitrage arrangements. Nor do the factual and legal landscapes of the other cases cited by Old Republic bear any resemblance to the case at hand. (See *Demitropoulos v. Bank One Milwaukee, N.A.* (N.D.Ill. 1997) 953 F.Supp. 974, 985 [holding that automobile lessee's claim for interest on security deposit funds was unfounded: that secured lessor had use of funds to avoid borrowing or to increase lending on certain days did not constitute money received from collateral under Wisconsin law requiring secured party to remit the same to debtor or apply it to offset the debt]; *Turner v. General Motors Acceptance Corp.* (S.D.N.Y. 1997) 980 F.Supp. 737, 740 [earnings credits awarded by bank to automobile financing company, which could only be used to offset charges to maintain the company's account, were not equivalent of interest].)

2. *The Trial Court Correctly Determined that the Borrower Who Pays Interest on Lender Funds Deposited in Escrow Is Entitled to the Interest Earned on Those Funds*

a. *Introduction*

Old Republic obtained and retained illegal interest on lender funds through both its cost avoidance and arbitrage schemes. The trial court awarded 96 percent of the "lender float" to class members because "in 96% of the escrows where lender funds were deposited the buyer paid interest on or before the close of escrow." In other words, lenders deposit funds in escrow *for the use of buyer or refinancer*, and the consumer pays for the use of that money while it sits in escrow pending the close of escrow. Old Republic does not and cannot refute the substantiality of the evidence underscoring the court's finding. Economist Paul Regan testified that lenders charged the consumer interest in 96 percent of a representative sample of escrows.

Nonetheless, attacking the decision below, Old Republic argues that the lender is the depositing party entitled to interest under Insurance Code section 12413.5, and that as a general proposition of law interest follows principal. Moreover, until

escrow closes it is the lender, not the consumer, who owns the funds and is entitled to interest thereon.

b. *In This Situation the Borrower is the "Depositing Party to the Escrow"*

Insurance Code section 12413.5 states that no interest earned on funds deposited in connection with an escrow shall be transferred to the account of a title insurance, controlled escrow or underwritten title company. Thus, interest generated by lender escrow deposits *may not flow to ORTC*. The statute also provides that any interest received on funds deposited into escrow "shall be paid . . . to the depositing party to the escrow . . . ." (Ins. Code, § 12413.5.) The trial court ruled that the language "depositing party to the escrow" should be construed to include *both* lenders and borrowers, depending on the circumstances. If a borrower does not pay interest on lender funds prior to the close of escrow, the borrower has no right to any interest earned on those funds and the lender should be viewed as the depositing party entitled to the interest. But if lender has charged borrower interest on deposited lender funds prior to the close of escrow, the "borrower has paid for the use of the money and should be entitled to any interest earned on the deposit. Even if title to the funds remains with the lender until the close of escrow, the money should be regarded as having been deposited by the lender on behalf of the borrower since the borrower paid interest on those funds."

As the trial court correctly held, the term "depositing party to the escrow" as used in Insurance Code section 12413.5 is not constrained by an overly technical notion of ownership or title to deposited funds. Funds are placed in escrow by the lender *on behalf of the borrower, who is a party to the escrow*. Nothing in section 12413.5 precludes the correct and equitable result that when the borrower has paid the lender for the use of lender funds as they remain in escrow prior to closing, that use includes the right to any interest accrued on those funds while in escrow and therefore the borrower, not the lender or ORTC, is entitled to it.

c. *The Principle "Interest Follows Principal" is Inapposite*

Old Republic cites case upon case standing for the general rule that interest follows principal. This general rule has no application to the unusual facts of this case. The trial court was faced with potentially competing claims for interest (lender vs. borrower) on funds obtained by an escrow holder with no valid claim to such interest.

d. *The Restitution Order Was Sound*

The trial court entered an order for restitution of 96 percent of the lender float to class plaintiffs. Business and Professions Code section 17203 empowers the trial court to "make such orders or judgments . . . as may be necessary to restore to any person in interest any money or property, real or personal, which may have been acquired by means of such unfair competition." A UCL order for restitution compels the defendant to return money obtained through unfair competition "to persons who had an ownership interest in the property or those claiming through that person." (*Kraus v. Trinity Management Services, Inc*. (2000) 23 Cal.4th 116, 127, fn. omitted.) Old Republic asserts borrowers never owned the lender funds and thus, have no right to recoup interest thereon through restitution. We do not agree.

The issue here is whether the consumers who have paid interest on lender funds are persons "in interest" with respect to those funds. They are. As a general rule, the consumer-borrower has a contingent contractual interest in such funds in that lender has made a commitment to fund the transaction subject to the conditions necessary to close escrow. Otherwise, matters would not proceed to the point of the lender depositing funds in escrow and charging the borrower interest thereon. At that point, the borrower has paid for the use of those funds. California recognizes future, contingent interests. (See Civ. Code, §§ 688, 690, 697; *Estate of Zuber* (1956) 146 Cal.App.2d 584, 590-591.) Contrary to Old Republic's assertion, the borrower has more than an inchoate expectancy. On the other hand, the positions of an heir apparent designated in a will, and of a beneficiary named in an insurance policy subject to change by the insured, *are* mere expectancies. (*Thorp v. Randazzo* (1953)

41 Cal.2d 770, 773.) Mere possibilities such as these are not deemed to be an interest of any kind. (Civ. Code, § 700.) In contrast, here the lender has a contractual commitment to fund, subject to borrower's performance and other conditions of escrow. The lender cannot unilaterally withdraw funding for any reason, without facing contractual consequences.

For all these reasons, we conclude that borrowers and refinancers who paid interest on lender funds are persons in interest within the meaning of Business and Professions Code section 17203 with respect to the lender float. Therefore, the restitution order awarding them interest earned thereon was sound.

B. *Class Plaintiffs' and The People's Issues Against Old Republic*

1. *Class Plaintiffs' Certification Concerns*

a. *Standard of Review*

Code of Civil Procedure section 382 authorizes class actions when "the question is one of a common or general interest, of many persons, or when the parties are numerous, and it is impracticable to bring them all before the court . . . ." To obtain certification, a party must establish "an ascertainable class and a well-defined community of interest among the class members." (*Linder v. Thrifty Oil Co*. (2000) 23 Cal.4th 429, 435.) The proponent of certification must show, among other matters, that "questions of law or fact common to the class predominate over the questions affecting the individual members . . . ." (*Washington Mutual Bank v. Superior Court* (2001) 24 Cal.4th 906, 913.)

Trial courts are afforded great discretion in granting or denying class certification. (*Linder v. Thrifty Oil Co.*, *supra*, 23 Cal.4th at p. 435.) We will reverse an order granting or denying class certification if it is based on improper criteria or erroneous legal assumptions, even though substantial evidence may support the court's order. (*Id*. at pp. 435-436; *Corbett v. Superior Court* (2002) 101 Cal.App.4th 649, 658.) Any pertinent, valid reason is sufficient to uphold the order. (*Linder v. Thrifty Oil Co., supra,* 23 Cal.4th at p. 436.) Moreover, our Supreme Court has admonished trial courts to weigh the benefits and burdens of class actions and permit

them only where substantial benefits accrue to litigants *and* the courts. (*Id*. at p. 435.)

b. *The Trial Court Correctly Excluded Subescrows From the Class*

Ruling on class plaintiffs' motion for class certification, the trial court determined that the class definition should "be limited to customers who had escrows directly with [ORTC]." During oral argument on the motion, the court also indicated that if ORTC were "keeping secret interest in the Southern California model, it is secret interest that belongs to a lending institution and not secret interest that is owed to the customer. It's not the customer's money yet. And that seems to me to be the reason for which the customer in [the] Los Angeles scenario would not be a proper class member." Class plaintiffs are adamant that we must overturn the class definition ruling, asserting that the court prematurely excluded ORTC's subescrows in Southern California at the certification stage of the proceedings. In effect they argue the court prejudged their entitlement to interest on lender funds because the court ultimately arrived at an opposite conclusion with respect to those borrowers who paid interest on lender funds.

An understanding of how ORTC operates in Southern California is helpful. There, escrow transactions are typically handled by independent escrow companies. Buyers, sellers and lenders alike contract directly with the escrow company for escrow services. The parties to a transaction address their escrow instructions to the escrow company, which in turn performs the instructions without any involvement of companies such as ORTC. Buyers, sellers and borrowers have no direct contact with ORTC. However, lenders deposit their funds with ORTC. This latter arrangement is called a subescrow, although it is a depositary relationship and not an escrow. A senior vice-president of Old Republic declared that lenders often are "unwilling to deliver loan funds to independent escrow companies because those companies frequently lack the size or longevity associated with solvency and liquidity." Thus, they insist on depositing their funds with a company such as ORTC.

Attacking the trial court's ruling excluding subescrows from the class, class plaintiffs ignore the main thrust of the certification proceeding which focused primarily on the contours of the class pursuant to their own proposed definition. In their moving papers, class plaintiffs defined the class as constituting "[a]ll persons and entities who were parties to escrows conducted by or through the Defendants or their affiliates and who . . . did not receive interest earned on their deposits." The trial court noted that in Southern California, buyers were parties to escrows conducted through independent escrow companies, not ORTC. The situation in Southern California was very different because the buyers were not customers of ORTC and had not entered into any agreements with ORTC. Thus, as the court asked, how could one say "that Old Republic somehow is withholding anything from the customer when it's not their customer"?

Any pertinent valid reason stated will be sufficient to uphold an order denying class certification. (*Linder v. Thrifty Oil Co.*, *supra*, 23 Cal.4th at p. 436.) Here, plaintiffs' complaints, and their proposed class definition, were grounded on a direct contractual escrow relationship. This significant common Northern California element was lacking in the lender subescrow situation. The Southern California buyer would be seeking restitution from ORTC, but that buyer was not ORTC's customer and had never signed and delivered escrow instructions to ORTC. Nor did ORTC have a depositary relationship with these individuals. The trial court did not abuse its discretion in limiting the class to ORTC's customers, particularly in light of class plaintiffs' own pleadings and proposed class definition, and the obvious differences between Southern and Northern California escrow practices.

c. *Nor Did The Trial Court Err in Limiting the Class Period*

i. *Introduction*

Actions under the UCL must be brought within four years of accrual of the cause of action. (Bus. & Prof. Code, § 17208.) Class plaintiffs argued below that the appropriate class period should encompass the entire period of Old Republic's cost avoidance activities, from 1978 to the present. They contended that the class

definition could not legally rest on a determination of the merits of any potential statute of limitations defense. Following a hearing, the court certified a plaintiff class for the period beginning four years prior to the filing of the first class action, namely July 24, 1994. Class plaintiffs assail this ruling.

ii. *Analysis*

(A) *Proper Weighing*

Here the trial court engaged in the necessary weighing, determining that substantial benefits would not accrue from extending the class period beyond the Business and Professions Code section 17208 limitation period where: (1) individual restitution awards would be small; (2) the purpose of Business and Professions Code section 17200 would be met without "go[ing] back to the beginning"; (3) an extended class would be unmanageable; and (4) the statute of limitations defenses would open the door to thousands of individual factual determinations.

Class plaintiffs take issue with the court's observance that individual recoveries would be small, pointing out that the very purpose of class action litigation is to provide a remedy where the loss to each individual member is small. The trial court did not ignore this principle. It merely recognized that as part of the balancing process, opening the class period beyond the four years would not appreciably benefit plaintiffs.

This concern is not new. Nearly 30 years ago our Supreme Court advised: "[W]hen potential recovery to the individual is small and when substantial time and expense would be consumed in distribution, the purported class member is unlikely to receive any appreciable benefit. The damage action being unmanageable and without substantial benefit to class members, it must then be dismissed." (*Blue Chip Stamps v. Superior Court* (1976) 18 Cal.3d 381, 386; *Caro v. Procter & Gamble Co.* (1993) 18 Cal.App.4th 644, 657-659.)

On the other hand, by allowing a discrete class action to proceed for restitution of illegal interest, along with the government enforcement action for penalties and other relief, the trial court vindicated the policies underlying Business and

Professions Code section 17200 while keeping its eye on the point of diminishing returns in terms of the benefit to the court. The court was well aware that a proposed class suit was not the sole means of deterring the unfair business practices or preventing unjust advantage to Old Republic. (See *Washington Mutual Bank v. Superior Court, supra*, 24 Cal.4th at p. 926.) Under the UCL the court can, and did, order injunctive relief and assess civil penalties. (Bus. & Prof. Code, §§ 17203, 17206.)

Finally, the court also properly weighed the burden of proliferation from thousands of individual showings that potentially would have to be made to establish delayed discovery or fraudulent concealment of their cause of action. Under the common law delayed discovery rule, the accrual of a plaintiff's cause of action is delayed to the time the plaintiff suspects or should have suspected wrongdoing which caused the injury. Where, as here, it is clear that the cause of action would be barred without the benefit of the delayed discovery rule, the plaintiff must show the inability to have made an earlier discovery despite reasonable diligence. (*McKelvey v. Boeing North American, Inc.* (1999) 74 Cal.App.4th 151, 160.) Similarly, a defendant's fraud in concealing a cause of action will toll the applicable statute of limitations, but to take advantage of this doctrine the plaintiff must show the substantive elements of fraud and an excuse for late discovery of the facts. (*Snapp & Associates Ins. Services, Inc. v. Robertson* (2002) 96 Cal.App.4th 884, 890.)

Class plaintiffs brush off the individualized inquiry concern but we are not persuaded that this concern can be ignored. The discovery rule analysis entails inquiry into whether the plaintiff had actual knowledge of the wrongful conduct, not just whether he or she "should have known" about it. As the trial court recognized, the actual knowledge component is fact-specific depending on the plaintiff's knowledge, experience, profession, etc. Thus, the inquiry proceeds on an individual basis. So, too, the inquiry for fraudulent concealment is also two-tiered: whether a reasonably diligent consumer would have discovered Old Republic's wrongdoing, as well as whether a particular class member is on inquiry notice of the claim. (See

Barber v. Superior Court (1991) 234 Cal.App.3d 1076, 1083.) Again, this is an individual inquiry.

In the last analysis, the issue is whether the trial court abused its discretion in impliedly concluding that certification beyond the limitation period would unduly impact the community of interest requirement for maintaining the class. As we have explained, it did not.

(B) *Massachusetts Mutual Does Not Aid Class Plaintiffs*

Class plaintiffs rely on *Massachusetts Mutual Life Ins. Co. v. Superior Court* (2002) 97 Cal.App.4th 1282 (*Massachusetts Mutual)* in their bid for this court to reject the trial court's reasoning in this case. There, the reviewing court *upheld* certification of a 33,000-member class comprised of persons who had purchased a particular life insurance product over a 15-year period. (*Id*. at p. 1286.) In so doing, the court rejected Massachusetts Mutual's contention that its statute of limitations defenses under Business and Professions Code section 17208 and another statute would require individual factual determinations. The court noted that the applicable limitations periods "*probably* [would] run from the time a reasonable person would have discovered the basis for a claim." (*Massachusetts Mutual, supra,* at p. 1295, italics added.) Further, "[g]iven the fact that plaintiffs' claim is based on a nondisclosure, the objective determination of when the nondisclosure should have been discovered seems readily amenable to class treatment. [¶] . . . '[C]ourts have been nearly unanimous . . . in holding that possible differences in the application of a statute of limitations to individual class members . . . does not preclude certification of a class action so long as the necessary commonality and . . . predominance are otherwise present.' " (*Ibid*.)

First, it bears noting that the *Massachusetts Mutual* court declined to disturb an existing order, as opposed to reversing a decision after the trial court thoughtfully balanced competing concerns. Second, glossing over concerns about individualized inquiries, the court overlooked the possibility that discovery and fraudulent concealment inquiries can also extend to what the claimant actually knew.

Moreover, at least one court has not been so quick to conclude that individual limitations issues do not overwhelm common issues. (See *Kapsimallis v. Allstate Ins. Co*. (2002) 104 Cal.App.4th 667, 674-675, fn. 6 [holding that determinations concerning delayed discovery allegations "must be made by individual fact-specific inquiries" and that trial court would have to decide on remand "whether these required individual fact-specific inquiries preclude class certification"].)

In any event, we underscore that class certification was not denied outright. Rather, the court merely limited the definition of the class period. The possible proliferation of individual inquiries was but one of several considerations the trial court assessed in weighing whether a broader certification period would substantially benefit litigants *and* the court. The court was also concerned with the burden of managing a class with thousands upon thousands of more plaintiffs, to whom little benefit would accrue. The practical reality of the impact on the court system did not escape comment. "[T]o go back to the beginning . . . you exceed the breaking point." Moreover, constricting the certification period did not contravene the Business and Professions Code section 17200 policies and indeed other remedies were and are available to vindicate those concerns. We therefore conclude that the court did not resort to improper criterion or legal assumptions in restricting the class based on these practical, manageability issues.

(C) *Other Doctrines Do Not Compel a Different Result*

Nor, as class plaintiffs suggest, do the doctrines of continuing violation or last overt act aid them. The continuing violation doctrine comes into play when a plaintiff's claim is based on conduct occurring, in part, outside the limitations period. It is routinely invoked in the employment discrimination context. (See *Richards v. CH2M Hill, Inc*. (2001) 26 Cal.4th 798, 812-821.) As articulated in *Richards*, when an employer engages in a continuing course of illegal conduct that does not constitute constructive discharge, the statute of limitations begins to run when the course of conduct ends or the employee is on notice that further efforts to end the conduct will be in vain. (*Id*. at p. 823.) Moreover, a challenge to a systemic policy of

discrimination is always timely when launched by a *present employee* even though events evidencing its inception occurred prior to the limitations period. The rationale is that the very existence of the continuing system of discrimination is what deters the employee from seeking full employment rights or threatens to adversely affect him or her in the future. (*Morgan v. Regents of University of California* (2000) 88 Cal.App.4th 52, 64.) Application of the continuing violation theory only makes sense in the context of an individual's current experience with respect to the policy or conduct. It is not a tool to bring in *new* people who suffered the harm prior to the limitations period.

Similarly, when liability is premised on a civil conspiracy the statute of limitations does not commence "until the 'last overt act' pursuant to the conspiracy has been completed." (*Wyatt v. Union Mortgage Co*. (1979) 24 Cal.3d 773, 786; see *Molko v. Holy Spirit Assn*. (1988) 46 Cal.3d 1092, 1127.) This doctrine will not assist plaintiffs against Old Republic. Conspiracy is "a legal doctrine that imposes liability on persons who, although not actually committing a tort themselves, share with the immediate tortfeasors a common plan or design in its perpetration. [Citation.] By participation in a civil conspiracy, a coconspirator effectively adopts as his or her own the torts of other coconspirators within the ambit of the conspiracy. [Citation.] In this way, a coconspirator incurs tort liability co-equal with the immediate tortfeasors." (*Applied Equipment Corp. v. Litton Saudi Arabia Ltd*. (1994) 7 Cal.4th 503, 510-511.) Here the trial court granted Old Republic's motion for summary judgment on plaintiffs' conspiracy (RICO) claim and they have not appealed that part of the judgment. Old Republic is the "immediate" wrongdoer under the UCL, but there is no actionable conspiracy.

(D) *The Disgorgement Ruling Will Stand*

Class plaintiffs further contend that the trial court should have ordered Old Republic to disgorge the approximatelty $1,165,000 restitution payment which Barr made to Old Republic in 1998, representing a portion of cost avoidance benefits illegally obtained through CEB. Although this payment was made to Old Republic

during the class period as defined by the court, the court nonetheless declined to order disgorgement because the funds "were earned on deposits in escrow accounts in existence prior to the class period. Accordingly, any claim on theses funds is barred by the four year statute of limitations . . . ."

Class plaintiffs argue that Old Republic's liability did not arise under Insurance Code section 12413.5 with respect to interest earned on escrows represented by this payment until Old Republic actually received those funds and then failed to pay them over to its customers. Regardless of when liability *arose*, class plaintiffs had no claim for restoration of such funds because they were not harmed by chicanery which occurred before they were ever parties to ORTC's escrow accounts. (See Bus. & Prof. Code, § 17203 [providing for restoration of money or property acquired by means of unfair competition].) As we find the trial court did not err in restricting the class period, so, too, it did not err in ruling that Barr's restitutive payment was beyond class plaintiffs' reach.

2. *The Trial Court Appropriately Restricted the People's Claim to the Four-year Limitation Period*

The People urge that the trial court should have applied the discovery rule and the fraudulent concealment doctrine to expand the applicable statute of limitations for the government's UCL claim. Additionally, they claim the four-year limitation period does not and should not curtail the court's ability to impose penalties for conduct occurring prior to that period.

a. *The People Waived Reliance on Equitable Doctrines*

As we explain, the People have waived any claim that regardless of the definition of class period, the equitable doctrines of delayed discovery and fraudulent concealment should have been applied to the government enforcement action.

In the original complaint the People sought penalties, injunctive relief, restitution and disgorgement of ill-gotten gains with respect to the UCL claim. The People also alleged fraudulent concealment and late discovery. However, after the class actions were filed they abandoned any separate quest for restitution, stating in

their trial brief: "The People would support restitution through a class claim recovery."

Nor did the government participate in the debate about whether to extend the class period beyond the four-year statute of limitations. Lawyers for the City appeared at the status conference where certification issues were discussed and the schedule was established, and received the schedule for numerous matters including the briefing schedule for determining the statute of limitations for the class period. They also appeared at the hearing. Nonetheless, the government lawyers neither spoke, nor wrote, a word on the matter until the court below invited the governmental plaintiffs to review the penalty assessed against ORTC for unlawful reconveyance fees, as set forth in the court's tentative decision regarding remedies. Responding by letter brief to the court, the government lawyers did not mention equitable doctrines. Rather, they contended that the four-year statute of limitations applied only to the period within which a UCL claim could be brought, but that penalties could be based on conduct occurring years prior to that term. In sum, the People have waived any argument that they could circumvent the four-year limitation period by invoking equitable doctrines.

b. *Penalties Are Not Available for Conduct Occurring Outside the Limitations Period*

Nor do we find merit in the People's argument that the trial court improperly transposed the class period onto the government action for penalties. They reason that their action is not a class action, and suffers none of the restrictions germane to the class procedure. We agree that UCL actions brought by a prosecutor are fundamentally different from representative or class actions brought by private parties. Nor do they require the same safeguards. (See *People v. Pacific Land Research Co.* (1977) 20 Cal.3d 10, 17-19.) "An action filed by the People seeking injunctive relief and civil penalties is fundamentally a law enforcement action designed to protect the public and not to benefit private parties. . . . Civil penalties, which are paid to the government [citations] are designed to penalize a defendant for

past illegal conduct. The request for restitution . . . is only ancillary to the primary remedies sought for the benefit of the public." (*Id*. at p. 17; accord, *Payne v. National Collection Systems, Inc*. (2001) 91 Cal.App.4th 1037, 1045.)

The structure of the UCL underscores this distinction. Only government prosecutors acting "in the name of the people of the State of California" may pursue remedies under Business and Professions Code section 17206. (*Id.*, subd. (a).) And the "People of the State of California" are harmed by the very existence of unlawful, unfair and fraudulent business acts and practices, whether or not individual citizens rely on a defendant's falsehoods or are affected by its illegal practices. (See *Prata v. Superior Court* (2001) 91 Cal.App.4th 1128, 1146.)

However, does this distinction make any difference when it comes to recovering penalties for specific violations subject to the UCL? No. The only court confronting a potentially similar issue declined to render a decision on this point. In *Suh v. Yang* (N.D.Cal. 1997) 987 F.Supp. 783, 795, involving allegations of multiple, continuous wrongful acts involving use and dilution of a service mark, the court concluded the plaintiff's claim for unfair competition was not barred by the Business and Professions Code section 17208 limitation period because some of the acts transpired during that period. However, the court did not address the question whether the plaintiff could *recover* for allegedly infringing acts occurring *outside* the four-year statute of limitation issue because the parties did not raise that concern. (*Suh v. Yang, supra,* at p. 796, fn. 9.)

As in *Suh v. Yang, supra,* there is no question but that the government's UCL action was timely. However, here the trial court answered the question left open in *Suh* with a "no," ruling that violations occurring outside the Business and Professions Code section 17208 period may not be counted for purposes of imposing a per-violation penalty. Such treatment "would be contrary to the well established purpose of a statute of limitation."

We agree. Even though ORTC's pattern of conduct was systemic and the violations numerous, the government is seeking penalties for discrete violations

dating back to the early 1980's. Statutory penalties are mandatory in actions brought in the name of the People, and they are imposed on a *per-violation* basis. (Bus. & Prof. Code, § 17206, subd. (a).) Had the government launched its UCL action earlier, doubtless the offending behavior and sheer magnitude of illegal acts would have been curtailed along with the accrual of penalties. There is a fairness issue here. The government will argue it could not have commenced its action earlier because it did not reasonably discover the wrongful behavior until 1994. Again, the government has waived delayed discovery and fraudulent concealment claims with respect to the limitation period for its own action.

More importantly, as a general matter government UCL actions will often be aimed at a pervasive practice harmful to consumers that can be segmented into independent violations. For the statute of limitations to have any meaning or effect, it should operate to cut off stale violations. Indeed, other courts have calculated penalties in UCL actions based on the four-year statute. (See, e.g., *South Bay Chevrolet v. General Motors Acceptance Corp*. (1999) 72 Cal.App.4th 861, 874, fn. 8.) This does not mean, however, that the UCL's deterrent purpose is not served with respect to those violations. Under Business and Professions Code section 17206, subdivision (b), in assessing the amount of the penalty to be imposed for each violation, among other matters the court may consider the number of violations, the persistence of the defendant's conduct and the length of time over which the misconduct occurred. Thus, violations occurring outside the limitations period can bear on the gravity of the penalty imposed for violations occurring within the limitations period.

3. *The Disbursement Float Ruling Was Correct*

For purposes of this lawsuit, the "disbursement float" "is comprised of funds remaining in the bank account after disbursement checks have been issued upon the close of escrow prior to the checks having been presented to the bank for payment." Concerning the disbursement float, the trial court ruled that: (1) Insurance Code section 12413.5 does not entitle nondepositing sellers to interest earned on escrow

funds, and in any event sellers were not part of the class entitled to restitution; (2) buyers' interest in escrow funds is extinguished at the close of escrow; and (3) as a limited agent, once ORTC issues checks to pay escrow obligations, it has satisfied its obligations to the escrow parties and is entitled to retain any benefit earned on funds while awaiting clearance of the payment.

Class plaintiffs dispute these rulings. They argue sellers are class members as well as depositing parties under Insurance Code section 12413.5, and in any event homeowners in refinancing transactions are depositing parties entitled to interest earned after the close of escrow. Further, they are adamant ORTC cannot be permitted to keep *any* interest and even if the trial court ruling was correct under the "unlawful" prong of Business and Professions Code section 17200, ORTC's conduct was improper under the "unfair and fraudulent" prong. The People argue that the issue of who is or is not within the class has no bearing on their case under the UCL and at the very least, the disbursement float should be disgorged to a *cy près* fund.

We need not belabor each of these points because we conclude that Insurance Code section 12413.5 ceases to govern the rights of the escrow parties and the escrow obligations of ORTC *before* any disbursement float begins to accrue. Specifically, ORTC's escrow duties are extinguished and the parties to the escrow have received all to which they are entitled at that point of convergence in time when: (1) the conditions specified in the escrow instructions have been satisfied; and (2) ORTC disburses the escrow funds in accordance with those instructions.

a. *The Escrow Process*

A brief description of the escrow process is in order. Our Insurance Code defines an "escrow account" as follows: "[A]ny depository account with a financial institution to which funds are deposited with respect to any transaction wherein one person, for the purpose of effecting the sale, transfer, encumbering or leasing of real or personal property to another person, delivers any written instrument, money, evidence of title to real or personal property . . . to a third person to be held by that third person until the happening of a specified event or the performance of a

prescribed condition, when it is then to be delivered by that third person to a grantee, grantor, promisee, promisor, obligee, obligor . . . ." (Ins. Code, § 12413.1, subd. (f).)

In practical, real estate parlance, an escrow "open[s]" with the deposit of initial instructions and is "closed" when the sale or refinancing is complete and the conditions satisfied. (3 Miller & Starr, Cal. Real Estate (3d ed. 2000) § 6:1, p. 4.) When the conditions of escrow have been performed fully, title and purchase money pass to the grantee and grantor respectively, as a matter of law, even though there has been no delivery. (*Hagge v. Drew* (1945) 27 Cal.2d 368, 375.) The same would be true in a refinancing situation.

The escrow holder is a limited agent whose duties extend to the strict and faithful performance of the principal's escrow instructions. (*Hannon, supra*, 211 Cal.App.3d at pp. 1127-1128.) Once the escrow holder receives instructions and the respective deposits of instruments and money from each party, the agent holds the money and instruments as agent of both parties to the escrow. (*Shreeves v. Pearson* (1924) 194 Cal. 699, 707.) The agent has no authority to deliver or dispose of the instruments and funds placed in escrow until the escrow conditions have transpired according to the terms of the instructions. (*Love v. White* (1961) 56 Cal.2d 192, 194; *Todd v. Vestermark* (1956) 145 Cal.App.2d 374, 377.)

Funds received by a company in connection with an escrow must be deposited in a separate account with a financial institution. (Ins. Code, § 12413.5) Any item received in connection with an escrow must be deposited in, or submitted for collection to, a financial institution no later than the close of the next business day following receipt. (*Id*., § 12413.2.) Where the buyer, refinancer or buyer's lender deposits the requisite payment into escrow by check, the condition of payment is satisfied when the check is honored by the drawee bank and funds have thus become available for withdrawal as a matter of right. (See *Greenzweight v. Title Guar. & Tr. Co*. (1934) 1 Cal.2d 577, 581-582; 3 Miller & Starr, Cal. Real Estate, *supra*, § 6:18, pp. 41-42.)

Also pertinent to the escrow process is Insurance Code section 12413.1, which establishes uniform holding periods governing when title insurance, controlled escrow and underwritten title companies can disburse various types of funds from escrow accounts. For example, under the statute, funds deposited by cash or electronic payment may be disbursed on the same day as the deposit. (Ins. Code, § 12413.1, subd. (c).) Deposits other than cash or electronic payments which are accorded next-day availability pursuant to 12 Code of Federal Regulations part 229 (2004) (Regulation CC)[35] may be disbursed the business day *after* the business day of deposit. (Ins. Code, § 12413.1, subd. (a).) These items include cashier's, certified or teller's checks, postal money orders and the like where the aggregate amount of deposits is $5,000 or less. (12 C.F.R. §§ 229.10(c)(1)(v), 229.13(b).) Other than drafts, deposits which *are not* accorded next day availability under Regulation CC, such as personal or business checks, may be disbursed when funds are made available for withdrawal according to that regulation. (Ins. Code, § 12413.1, subd. (b).)[36] Funds cannot be disbursed with respect to a draft, other than a share draft, until the draft has been submitted for collection and payment received. (*Id.*, § 12413.1, subd. (e).)

When all the conditions pending escrow have been performed within the required time, the dual agency of the escrow holder converts to an agency for each of the parties to the transaction in respect to those items deposited in escrow to which each has become "completely entitled." (*Shreeves v. Pearson, supra,* 194 Cal. at p. 707; *Todd v. Vestermark, supra,* 145 Cal.App.2d at p. 377.) At this point,

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[35] Regulation CC governs availability of funds deposited in "insured banks" and other financial institutions. (12 C.F.R. § 229.2(e).) An insured bank is any bank, including a state bank, whose deposits are insured under the Federal Deposit Insurance Act. (12 C.F.R. § 229.2(e); 12 U.S.C. § 1813, subds. (a)(1)(A), (h).)

[36] Nonetheless, such funds can be disbursed on the business day after the business day of deposit if the depositary institution advises the title insurance, controlled escrow or underwritten title company in writing that final settlement has occurred. (Ins. Code, § 12413.1, subd. (d).)

consistent with Insurance Code section 12413.1 and the escrow instructions, the title insurance, controlled escrow or underwritten title company, acting, for example, as agent of seller, would deliver funds to seller. And, at the moment of disbursement, all relevant deposits with respect to a given escrow are either cash or the functional equivalent of cash; deposits accorded final settlement or, in the case of a draft, for which payment has been received; or funds defined by Regulation CC as available for withdrawal. In other words, these funds are good funds in the hands of the escrow holder by virtue of the operation of Insurance Code section 12413.1.

b. *Analysis*

While buyers and refinancers have title to the deposited funds *until* close of escrow, their interest in such funds ceases upon disbursement by the company in accordance with the escrow instructions. At that time the buyer has title to the property and the refinancer takes title as reflected in the refinancing transaction. Thus after closing buyer and refinancer have no funds that can float. Nor do they have an account to amass interest because the title insurance, controlled escrow or underwritten title company—not any party to the escrow—owns the escrow disbursement account. Finally, upon disbursement the seller has what he or she is entitled to under escrow instructions providing that all disbursements shall be by check of ORTC and pursuant to which buyer and refinancer acknowledge that escrow funds must be disbursed in accordance with the provisions of Insurance Code section 12413.1. Should seller so choose, seller should be able to pick up ORTC's check on the date of disbursement and cash it that day at ORTC's depository bank. (See 12 C.F.R. § 229.2(d) [defining "available for withdrawal" with respect to funds deposited in an account as including available "for payment of checks drawn on the account"].)

Therefore, upon transfer of documents and issuance of disbursement checks in strict accordance with the escrow instructions, ORTC's escrow obligations are

extinguished and Insurance Code section 12413.5 no longer applies.[37] Nonetheless, class plaintiffs argue that Insurance Code section 12413.5 continues to govern the transaction "until good funds are disbursed" and ORTC continues as a separate agent of buyer, seller and refinancer until funds are *actually* received by the seller. Again, as a general matter Insurance Code section 12413.1 ensures that only good funds are disbursed.[38] After disbursement, the title insurance, controlled escrow or underwritten title company, as a corporate entity, has an obligation to honor its own checks, but its escrow obligations have been accomplished. " '[T]he obligations of an escrow agent are limited to faithful compliance with the instructions from the principals.' " (*Hirsch v. Bank of America*, *supra*, 107 Cal.App.4th at p. 719.) Moreover, the title company's role as separate agent of seller upon satisfaction of the conditions of escrow is still circumscribed by the instructions, and terminates upon completion of performance of the acts required thereby. (*Claussen v. First American Title Guaranty Co*. (1986) 186 Cal.App.3d 429, 435.) Again, the instructions require disbursement by check, in accordance with Insurance Code section 12413.1.

Nor are we persuaded by class plaintiffs' continued intonement that the right to interest follows the principal and, thus, sellers or buyers, by permission of sellers who accept disbursement by check, are entitled to the disbursement float. First, the cases they rely on have nothing to do with the disbursement float. (See, e.g., *Phillips v. Washington Legal Foundation* (1998) 524 U.S. 156. 165 [interest earned on client trust funds held in IOLTA accounts]; *Metropolitan Water Dist. v. Adams* (1948) 32

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[37] For this same reason, our language in *Hirsch*, that as between title companies and their customers, Insurance Code section 12413.5 "dictates that the customers have the superior right to any payments made by Banks that constituted interest" does not affect entitlement to interest when Insurance Code section 12413.5 no longer applies. (*Hirsch v. Bank of America,, supra*, 107 Cal.App.4th at p. 718.)

[38] Companies are not liable for any violation of Insurance Code section 12413.1 if the violation is unintentional or the result of a bona fide error. (§ 12413.1, subd. (i).) Moreover, the parties can consent in writing to recordation of documents prior to the time funds are available for disbursement with respect to a transaction. (*Id*., subd. (j).)

Cal.2d 620, 628-629 [interest earned on water district funds deposited with court as security for commencing eminent domain proceedings].) Second, we concur with the trial court that the authority pertaining to this issue supports ORTC's entitlement to retain the disbursement float. In particular, in *Van de Kamp v. Bank of America* (1988) 204 Cal.App.3d 819, 852-853 the bank issued checks to pay trust obligations issued from a central disbursing account and immediately charged the trust account. Pending clearance, the funds to cover the check were placed in a pool available to the bank for use. The reviewing court upheld the trial court's finding that this practice " 'accords with generally accepted accounting principles and is an application of the rule permitting a trustee to keep cash on hand to pay upcoming expenses of the account. The obligation of the trust, for which the check is issued, is extinguished and becomes [bank's] obligation. The trust check is virtually the same as a cashier's check . . . , is almost a form of money and may be cashed immediately. Hence, [bank] must ensure that it has funds available for payment of the check at the time it is issued.' " (*Id*. at p. 852.) The record supported the finding that the use of the disbursing float was reasonably necessary to the orderly administration of the trust accounts, and the court concluded there was no obligation to return the value of its use to the trust beneficiaries. (*Id*. at p. 853.) An escrow is similar. Upon disbursement of good funds, the title company's escrow obligations are fulfilled but the company now has a corporate obligation to maintain appropriate balances pending clearance of payment on disbursement checks. It is of no legal consequence that unlike the bank, the ORTC is not statutorily empowered to self-deposit the applicable funds, or use a separate disbursement account.

Finally, we reject class plaintiffs' argument that even if ORTC's retention of the disbursement float was "lawful" under Insurance Code section 12413.5, it was "unfair" or "fraudulent" within the meaning of Business and Professions Code section 17200. First, ORTC's escrow obligations and agency terminated upon disbursement of good funds. Second, class plaintiffs' related complaint that ORTC failed to advise depositors they could open an individual interest-bearing account

does not bear on the issue of Old Republic's retention of interest on the disbursement float. This failure to advise, appropriately addressed in the court's injunctive relief measures, is not a proper vehicle for *restitution* under the facts of this case. Third, although ORTC's form escrow instructions dictate that disbursements shall be made by check, we are not convinced that this condition is detrimental to its customers. The trial court found, and class plaintiffs have not refuted, that there was no evidence suggesting that the reasonable cost of a wire transfer ordinarily would not exceed the interest accruing during the disbursement float. Thus, where is the detriment?

4. *The Trial Court Did Not Abuse Its Discretion in Fashioning the Injunctive Relief Order*

After the trial court rendered its decision on remedies, Old Republic submitted three alternative compliance plans and moved for approval. The trial court approved plans that would allow Old Republic to retain arbitrage benefits in the future, provided its escrow instructions fully and fairly disclosed this state of affairs and afforded the consumer the option of opening an individual interest-bearing account for which ORTC would charge a reasonable fee. These instructions also provided guidance on how to calculate estimated interest so the consumer could make an informed decision about whether to open an interest-bearing account. The court also found that the proposed fees for opening and maintaining an interest-bearing account and for facilitating wire transfers were "good faith estimate[s] of the actual cost" incurred.

We review the trial court's exercise of its injunctive powers pursuant to Business and Professions Code section 17203 under an abuse of discretion standard. (*Brockey v. Moore* (2003) 107 Cal.App.4th 86, 102-103.) Complaining that the relief ordered was insufficient because it allowed ORTC to retain arbitrage benefits on consumer escrow funds in the future, class plaintiffs first argue that the injunctive relief did not comply with Insurance Code section 12413.5. To reiterate, that statute provides that any interest received on escrow deposits shall be paid to the depositing party "unless the escrow is otherwise instructed by the depositing party, and shall not

be transferred to the account of the title insurance company, controlled escrow company, or underwritten title company." (Ins. Code, § 12413.5.) Class plaintiffs highlight the "shall not be transferred" phrase, but ignore the language allowing an alternative disposition upon instruction of the parties. That is what the revised escrow instructions accomplished.

Next, they disparage the basis of the court's order, namely that the cost of calculating and reporting each individual escrow depositor's share of arbitrage benefits on a pooled demand deposit account would be a logistical nightmare and cost-prohibitive. Although class plaintiffs submitted evidence that existing technology permitted tracking of the investability of funds deposited in a common general escrow account, the trial court also weighed Old Republic's argument that this procedure was untested, no one else was using it and Old Republic did not know if it was "doable." Plaintiffs are merely disagreeing with the court's assessment of the evidence. (See *Brockey v. Moore*, *supra*, 107 Cal.App.4th at p. 103.) But more fundamentally, the court correctly saw its role as fashioning injunctive relief to ensure that defendants were complying with existing law. Beyond that, even if plaintiffs' approach were feasible, the court had no authority to prohibit Old Republic from carrying out a proposed plan that was lawful.

C. *The People's Issues Against PwC*

1. *Introduction*

In the fourth amended complaint, the People alleged that PwC was legally required to, but did not, comply with generally accepted auditing standards (GAAS) in preparing the audit reports for ORTC. The trial court was not convinced that the alleged violations of auditing standards were actionable under the UCL, and therefore aborted the People's UCL claim against PwC on demurrer. Further, the court ruled that the People lacked a remedy because Old Republic had already escheated the unclaimed escrow funds to the State. The People object to these rulings.

The UCL broadly embraces anything properly identified as a business practice that simultaneously is forbidden by law. (*Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co*. (1999) 20 Cal.4th 163, 180 (*Cel-Tech*).) With its proscription of "any unlawful" business act or practice, the UCL transforms violations of other laws into independently actionable unlawful practices under its statutory umbrella. (*Ibid*.) It matters not whether the law violated is criminal, civil, federal, state, municipal, regulatory, statutory or court-made. (*South Bay Chevrolet v. General Motors Acceptance Corp*. (1999) 72 Cal.App.4th 861, 880.) And even if a practice is not specifically forbidden by another law, it may be deemed unfair or fraudulent under the UCL. (*Cel-Tech*, *supra*, 20 Cal.4th at p. 180.) To recover under this act, individualized proof of deception, injury or reliance is not necessary, nor is it necessary to prove that the defendant intended to injure anyone. (*Prata v. Superior Court*, *supra*, 91 Cal.App.4th at p. 1137.)

2. *Analysis*

The People's best argument is that PwC's alleged failure to comply with GAAS violated Business and Professions Code section 5062, which provides that accountants "shall issue a report which conforms to professional standards upon completion of a compilation, review or audit of financial statements." The California Board of Accountancy has issued regulations requiring accountants to "comply with all applicable professional standards, *including but not limited to* generally accepted accounting principles and *generally accepted auditing standards*." (Cal. Code Regs., tit. 16, § 58, italics added.) The complaint alleged numerous violations of GAAS in preparing and submitting "clean" audit reports for ORTC, based on PwC's alleged knowledge that (1) the company's inflated earnings from unescheated funds was material under GAAS; (2) the company's escheat practices were possible "illegal acts" by the client as defined by GAAS; (3) the company had never escheated money to the state as it was required to do; and (4) throughout the course of the engagement the company's total escheat obligation including penalties was growing. The complaint further alleged that the violations permeated the engagement in that year

after year PwC issued unqualified opinion letters for ORTC. These allegations were sufficient to state a cause of action under the UCL.

Nonetheless, PwC is adamant that limitations on accountants' liability articulated by our Supreme Court in *Bily v. Arthur Young & Co*. (1992) 3 Cal.4th 370 (*Bily)* are dispositive in this case and protect the company from suit under the UCL. We disagree.

The *Bily* court held that "an auditor's liability for general negligence in the conduct of an audit of its client financial statements is confined to the client, i.e., the person who contracts for or engages the audit services. Other persons may not recover on a pure negligence theory." (*Bily, supra,* 3 Cal.4th at p. 406, fn. omitted.) Despite the reality that economic injury to investors and others who might read and rely on audit reports is foreseeable (*id*. at pp. 398-401), the court deemed it necessary to curtail the pool of potential plaintiffs in order to avert "the spectre of multibillion-dollar professional liability that is distinctly out of proportion to" (1) the auditor's fault; and (2) the strength of the correlation between the defective report and a third party's injury (*id.* at p. 402). Additionally, the court was convinced that "the generally more sophisticated class of plaintiffs in auditor liability cases . . . permits the effective use of contract rather than tort liability to control and adjust the relevant risks through 'private ordering.' " (*Id*. at p. 398.) Furthermore, the court was not persuaded that a pure foreseeability approach would result in more accurate auditing and more efficient spreading of loss. (*Ibid*.) However, the court held that persons who are "specifically intended beneficiaries of the audit report who are known to the auditor and for whose benefit it renders the audit report," could recover on a theory of negligent misrepresentation. (*Id*. at p. 407.) Finally, auditors enjoy no protection against third party suits for intentional misrepresentation. (*Id*. at p. 415.)

Bily does not pertain. First, this is not a professional negligence action for damages; it is an action under the UCL for civil penalties, restitution and injunctive

relief[39] based on violations of GAAS. Contrary to PwC's assertions, allowing this lawsuit to proceed would *not* be "in flat contradiction of the *Bily* Court's refusal to 'endors[e] a broad and amorphous rule of potentially unlimited liability' for accountants." (Citing *Bily, supra*, 3 Cal.4th at p. 406.) Without the financial incentive of damages (including punitive damages) and attorney fees, and again contrary to PwC's assertions, it is unlikely that "*anyone*" would "sue *any* accountant for alleged failure to comply with GAAS in *any* audit." Injunctive relief and restitution are the only remedies available to individuals. (Bus. & Prof. Code, §§ 17203, 17206.) If an auditor engages in *ongoing* misconduct, injunctive relief would be appropriate; *Bily* would be no bar. (Bus. & Prof. Code, § 17203.) Likewise if the conduct results in acquisition by the auditor of "money or property, real or personal," by means of unfair competition, then restoration of the same to the person harmed is appropriate and again *Bily* would be no bar. (Bus. & Prof. Code, § 17203.)

PwC argues nonetheless that just as private plaintiffs cannot "plead around" the bar to the judicially implied private action against insurers who commit certain statutory unfair practices, as announced in *Moradi-Shalal v. Fireman's Fund Ins. Companies* (1988) 46 Cal.3d 287, 292, so too the People cannot "plead around" *Bily* by casting their claim as a UCL cause of action based on violations of GAAS. (See *Safeco Ins. Co. v. Superior Court* (1990) 216 Cal.App.3d 1491, 1493-1494 [holding that to permit plaintiff to prosecute UCL action would render *Moradi-Shalal v. Fireman's Fund Ins. Companies, supra*, 46 Cal.3d 287 meaningless].) There is no analogy here. *No* private party can sue for damages for the commission of unfair

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39 We agree with PwC that the People's UCL recovery is limited to civil penalties in the amount of $2,500 per violation. (Bus. & Prof. Code, § 17206, subd. (a).) The People did not assert ongoing misconduct, and thus injunctive relief is not available. Nor did the People allege that PwC benefited from ORTC's failure to escheat, and thus restitution is not available. (See *id.*, § 17203 [allowing for orders "as may be necessary to restore to any person in interest any money or property . . . which may have been acquired by means of such unfair competition"].)

claims settlement practices set forth in Insurance Code section 790.03, subdivision (h). (*Moradi-Shalal v. Fireman's Fund Ins. Companies*, *supra*, 46 Cal.3d at pp. 292, 304.) On the other hand, *Bily* does not obliterate any private right of action, but instead creates rules restricting who has standing to sue auditors for professional negligence. At most *Safeco* stands for the proposition that "the UCL cannot be used to state a cause of action the gist of which is absolutely barred under some other principle of law." (*Stop Youth Addiction, Inc. v. Lucky Stores, Inc*. (1998) 17 Cal.4th 553, 566.) There is no similar bar to the instant action.

Citing *Samura v. Kaiser Foundation Health Plan, Inc*. (1993) 17 Cal.App.4th 1284, 1299, PwC also complains that enlisting the UCL to police compliance with GAAS is tantamount to invading the powers entrusted by the Legislature to the Board of Accountancy, the entity with general power to regulate and discipline accountants in California. (Bus. & Prof. Code, § 5000 et seq.) *Samura* does not help PwC. First, our Supreme Court has held that despite the existence of a distinct statutory enforcement scheme, parallel action for unfair competition is appropriate under the UCL. (*People v. McKale* (1979) 25 Cal.3d 626, 632-633.) Second, the reviewing court in *Samura* held that the operative statutory provisions upon which the trial court relied in authorizing a UCL action *did not* define an unlawful act that could be enjoined as unfair competition. Rather, they served to govern the pertinent regulatory agency in the exercise of its regulatory powers. Thus, the lower court erroneously "assumed [a] regulatory power" that belonged exclusively[40] to a state agency. (*Samura v. Kaiser Foundation Health Plan, Inc.*, *supra*, 17 Cal.App.4th at pp. 1301-1302.)

Here, the statutory and regulatory provisions requiring accountants to comply with professional standards are not laws which serve to govern the Board of

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[40] At issue in *Samura* were provisions of the Knox-Keene Act. The court noted that the power to enforce that act "has been entrusted exclusively to the Department of Corporations, *preempting even the common law powers of the Attorney General*." (*Samura, supra*, 17 Cal.App.4th at p. 1299, italics added.)

Accountancy in its regulatory powers. They are general mandates setting the baseline standards for the conduct of the profession. Further, as suggested in *People v. McKale, supra*, 25 Cal.3d 626, the Board of Accountancy does not have exclusive authority to enforce provisions of the Business and Professions Code governing accountants: "The Accountancy Act (Bus. & Prof. Code, §§ 5000-5157) establishes the Board of Accountancy with authority to seek injunctive relief against violators of the act. (Bus. & Prof. Code, § 5122.) . . . [T]he district attorney is not expressly authorized to enforce the statute. While the issue has not been directly faced, it appears a concerned district attorney may prosecute an action for unfair competition predicated on violations of the Accountancy Act notwithstanding provisions for a special enforcement agency." (*People v. McKale*, *supra*, 25 Cal.3d at p. 633.)

Finally, even if *Bily* applied, here the People alleged that the DOI was the intended recipient of the auditor opinion letters. As a matter of law, when a company retains an outside auditor to satisfy its statutory requirement to file an audit report with the Commissioner under the Insurance Code, the Commissioner is within the universe of potential plaintiffs defined by *Bily*. (See *Arthur Andersen v. Superior Court* (1998) 67 Cal.App.4th 1481, 1501, 1507 [concerning Ins. Code, § 900.2, which requires insurers to file an annual audit report with the Commissioner].)

The Commissioner, duly elected by the People, also has regulatory and enforcement powers vis-à-vis underwritten title companies such as ORTC. (Ins. Code, §§ 12389 et seq., 12900, subd. (a).) PwC argues that " 'The People is not the Department of Insurance." This purported difference is meaningless. This UCL action was brought by public prosecutors authorized pursuant to Business and Professions Code section 17204 to sue "in the name of the People of the State of California." A suit in the name of the People represents the "sovereignty" of the state. (Gov. Code, § 100, subd. (a).) The Commissioner receives audit reports from underwritten title companies such as ORTC in the course of its enforcement and regulatory duties, which he or she performs for the benefit of the public, i.e., the

People. Thus, for all practical purposes the People's suit is indistinguishable from a suit by the Commissioner, an intended recipient of the allegedly offending reports.

IV. DISPOSITION

We affirm the trial court's rulings that the City is a person within the meaning of the FCA and the government's claims did not come within the public disclosure bar of that act. (Nos. A095918, A097793.) We also affirm the comprehensive judgment against Old Republic in its entirety. (No. A097793.) Parties to bear their own costs on that appeal. We reverse the summary judgment in favor of PwC on the government's FCA cause of action, as well as the dismissal of the People's UCL claim following the sustaining of PwC's demurer without leave to amend. (No. A095918.) PwC to pay costs of appeal.

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Reardon, J.

We concur:

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Kay, P.J.

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Sepulveda, J.

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Trial judge:	Hon. Stuart R. Pollak
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