

# CA Supreme Court Affirms the Use of Powerful Civil Theft Remedies Under Penal Code Section 496 in Business Tort Cases

*Tim Kowal* August 03, 2022



Civil trial attorneys have an industry secret. Say you are suing over an unpaid loan. If the borrower never intended to pay back the loan, that's not only a breach of contract, it's a form of theft by false pretenses. And under [Penal Code section 496](#), civil theft is punishable by treble damages and attorney fees. For those in on the secret, section 496 is a powerful tool in a business lawyer's toolkit.

One problem: courts really don't like section 496. They worry that lawyers will overuse it and turn every garden-variety loan or business-tort case into a civil theft case. So there arose a split of authority, with some cases enforcing section 496, and others refusing to enforce it.

Breaking the split, the California Supreme Court kept this powerful tool intact. In *Siry Investment, L.P. v. Farkhondehpour* (Cal. Jul. 21, 2022 No. S262081) 2022 WL 2840312, the Court [held](#) the civil theft remedies under section 496 applied to a case involving diversion of partnership cash.

But the Court did not throw open the floodgates. The Court noted that the concerns expressed by section 496 naysayers do “give pause.” And Justice Groban, joined by Justice Kruger, concurred to note they do not read the majority as endorsing civil theft penalties in “most consumer or commercial transactions.”

And on a separate point of civil procedure, the Court held that even a defaulted defendant may move for new trial to challenge excessive damages. **How the Defendants Turned a Moderately Bad Judgment Against Them Into a Very Bad Civil Theft Judgment**

*Siry Investment* involved familiar allegations about two partners diverting partnership assets to themselves via the various trust involved. The jury awarded about a quarter million in damages, plus punitives, reduced by the judge to about \$725,000 each.

Not a good outing for the defendants, but not devastating.

The defendants’ attorneys then raised a nice technical issue on appeal (the verdict form didn’t specify whether the award was against the defendant individually or as trustee), and got the judgment reversed and remanded for a new trial.

At this point, the defendants had a chance to salvage things. But they took their case in a different direction. They refused to respond to discovery. Then when the trial court ordered them to respond, the defendants refused to obey the court’s order, too.

So the plaintiff got terminating sanctions. And this time around, the plaintiff sought remedies under Penal Code section 496: treble damages and attorney fees.

And the plaintiff got them, too. The court entered judgment against the defendants for almost \$1 million in damages, almost \$2 million in treble damages (under section 496), \$4 million in punitive damages, \$4 million in fees (also under section 496), plus costs, for a total of over \$12 million.

Looking at the defendants’ case, by this point the wheels had come off. But the defendants still had a couple tricks up their sleeve.

First, the defendants moved for a new trial. And the trial court agreed that it could not award both treble damages and punitive damages. The plaintiff elected the remedy of treble damages. (An interesting choice, since punitives were \$4 million and treble damages were \$2 million. Probably a shrewd move by the plaintiff, knowing treble damages, being statutory, could not be challenged as excessive or lacking basis in financial condition.)

Ultimately, the trial court entered judgment against the defendants for over \$7 million.

Second, the defendants appealed the aspects of the judgment as improper under section 496. And the Court of Appeal agreed with them. Then, the Supreme Court granted review.

### **Defaulted Defendants May Still Challenge Damages Via a New Trial Motion**

The plaintiff cross-appealed from the order granting the defendants' motion for new trial, which had reduced the damages from \$12 million to \$7 million. But the Court rejected the plaintiff's argument.

The Court noted precedent holding that even a defaulting defendant—who has no right to participate at a prove-up hearing—nevertheless may appeal the default judgment on certain grounds. So the Court reasoned that there is “ ‘no reason to preclude [defendants] from seeking a new trial (or, more precisely, a new judgment hearing)’ ” on those same grounds.”

Specifically, a defaulted defendant may move for new trial under Code of Civil Procedure section 657, subdivision 7, concerning “errors in law, occurring at the trial and excepted to by the party making the application.” Even though the defaulted defendant cannot “except” to the errors, the Court held that “for reasons of judicial economy defendants may be seen as having the right to move for a new trial under that subdivision.”

The Court declined to follow other authorities that suggested defaulting defendant may not file a motion for new trial under any circumstances.

### **Civil Theft Remedies Under Penal Code § 496 Are Available in Certain Business Tort Cases**

The defendants were not successful, however, in persuading the Court that the civil theft remedies under Penal Code section 496 were improper in this case.

The Court analyzed three Court of Appeal cases applying section 496. *Bell v. Feibush* (2013) 212 Cal.App.4th 1041 held that the civil theft remedies under section 496 did apply. In *Bell*, the defendant borrower asked to borrow money from the plaintiff on the false pretense he needed the money to settle a lawsuit concerning a related enterprise. As the loan was induced by false pretenses, section 496 applied.

True, the *Bell* court acknowledged, construing section 496 too broadly could turn all commercial cases into civil theft cases. But section 496 is “clear and unambiguous” when it refers to “receiv[ing] any property that ... has been obtained in any manner constituting theft or extortion, knowing the property to be so ... obtained....” Even other states followed California’s example and enacted their own versions of section 496 in an effort to reduce instances of civil theft.

But *Lacagnina v. Comprehend Systems, Inc.* (2018) 25 Cal.App.5th 955 declined to extend section 496 to wage-and-hour cases. Labor is not “property” subject to the statute.

Tipping things back in favor of enforcing section 496, *Switzer v. Wood* (2019) 35 Cal.App.5th 116 followed *Bell*. *Switzer* involved a joint venture between business partners. The court held that section 496 could apply to such cases.

Back to the facts at hand, the *Siry* Court followed the *Bell* and *Switzer* cases. The Court held that section 496 is “unambiguous.” Reversing the Second District Court of Appeal, the Court rejected the intermediate court’s view that the statute does not apply in “theft-related tort cases.”

The Court concluded: “A plaintiff may recover treble damages and attorney’s fees under section 496(c) when property has been obtained in any manner constituting theft.”

Here, the fact that the judgment on review was a default judgment made it easier to affirm the section 496 remedies: the defaulted defendants were deemed to have admitted the allegations of theft. But in cases where misrepresentations or unfulfilled promises “are made innocently or inadvertently,” the civil theft remedies under section 496 would not apply.

The Court also disagreed that following the text led to an absurd result. Section 496 still requires a *fraudulent intent* in obtaining *property*, so these limitations prevent statute from being invoked in every business tort. Besides, how could this interpretation be “absurd” when other states have looked on it with favor and implemented it in their own jurisdictions?

The Court did take the policy concerns seriously. But, the Court noted, “these policy issues have not been hidden from the Legislature's attention, nor are they new.” “Indeed, courts of other states have so construed their statutes even in the face of policy-based admonitions against unduly expanding such remedies.” The Colorado legislature, for example, has adopted a similar civil theft statute, and its Supreme Court has applied it even more broadly to employee breach of contract actions. There is no reason to presume our legislature is less nimble.

Lest there be any misinterpretation, Justice Groban, joined by Justice Kruger, concurs to say the majority opinion does not “create a sea change in the law.” Justice Groban specifically cautions against seeking section 496 remedies in cases involving wage and hour laws, false advertising laws such as the unfair competition law or Consumers Legal Remedies Act, warranty laws such as the Song-Beverly Consumer Warranty Act, or real estate or mortgage lending disputes. And he concludes: “I do not believe it is likely that section 496 will apply in most cases concerning consumer or commercial transactions, and I do not read the majority's opinion to suggest otherwise.”

## Takeaway

Section 496 is strong medicine in the right business tort case. Here, it took a \$1 million judgment and added a further \$6 million in treble damages and attorney fees. (The \$4 million in fees is another story.)

If you have a civil case involving fraud that amounts to something akin to theft by false pretenses, consider seeking remedies under Penal Code section 496(c). Do not get too creative. But under *Siry Investments*, policy concerns are no longer a valid basis to refuse to enforce section 496.

*This article was [originally published](#) on the website of [Thomas Vogele & Associates, APC](#).*

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