Filed 1/4/10 City of L.A. v. Conway CA2/5

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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION FIVE

CITY OF LOS ANGELES etc., Plaintiff and Respondent, v. LLOYD CONWAY et al., Defendants and Appellants.	B205763 (Los Angeles County Super. Ct. No. LC074589)

APPEAL from a judgment of the Superior Court of Los Angeles County. Richard A. Adler, Judge. Reversed.

Law Office of Bruce Adelstein, Bruce Adelstein for Defendants and Appellants.

Rockard J. Delgadillo, City Attorney, Lisa S. Berger, Deputy City Attorney; Richard M. Brown, General Counsel, for Plaintiff and Respondent.

In this action for fraudulent transfer (Civ. Code, § 3439.04), the City alleged that Lloyd Conway and George Piedra fraudulently transferred the assets of Titan Capital dba Valley Cab to themselves, in order to avoid liability to the City in an action entitled *City of Los Angeles v. Hernan Garcia*. The City prevailed after court trial. We reverse.

Facts

The City presented its case principally through Conway's and Piedra's deposition testimony,[1] the testimony of Bruce Ballanger, a Certified Public Accountant, and documents. The defense called Miles Gothelf, Titan's Certified Public Accountant, and Piedra and Conway.

This lawsuit was filed in May of 2006, but the events leading to it began in February 2000. At that time, Conway was chief executive officer of Titan and was its principal shareholder.[2] Piedra was on Titan's Board of Directors. Both Conway and Piedra worked at Valley Cab, although the City presented conflicting evidence on Piedra's title and role.

On February 19, 2000, a Valley Cab taxi was involved in a two-car accident which resulted in $78,124 in damage to a DWP pole and DWP equipment. The other car was driven by Hernan Garcia. According to evidence presented by the City, and Conway's and Piedra's testimony at trial, the police report on the accident established that Garcia was driving under the influence and was responsible for the accident. Based on the report, neither Conway nor Piedra believed that Titan had any liability in the accident.

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[1] As to Conway, the City read portions of a April 29, 2003 deposition taken in what counsel for the City referred to as "the DiConte matter," and portions of several depositions (February 2004; August 2006; August 2007) from proceedings which are not identified. As to Piedra, the City read from a June 2007 deposition, which seems to have been taken in this case.

[2] There was no evidence about other shareholders. In its brief, the City sometimes asserts that Conway was Titan's sole shareholder. In evidentiary support, it cites his deposition testimony that he was the primary shareholder.

Although Garcia at one point sought to blame the cab driver, neither Garcia nor his insurance company made any claim against Titan.

In February 2001, the City filed suit against Garcia. At some point, Garcia settled for $5,000.

By 2000, Titan had been doing business as Valley Cab for 15 or 20 years, but in 1999 and 2000, the business lost money. Conway put the loss at $100,000 a year, and both accountants testified to losses of $276,000 in 2000. As reflected by the financial statements Titan submitted to the City, which were introduced into evidence by the City, Conway lent Titan $933,128 over the years. The documents also showed that for the fiscal years ending on January 31, 1998 and on January 31, 1999, Titan's Valley Cab expenses were approximately $2 million a year. Both accountants testified that on January 31, 2000, Titan had $1.9 million in assets and the same amount in liabilities. At the relevant time, the taxi business was Titan's only business.

The City presented Conway's deposition testimony that Valley Cab typically paid $200,000 a year in accident claims. Other evidence in the record suggests a lower number, perhaps $88,000 a year. Piedra testified that Valley Cab might have had 10 or 15 accidents in a good year, and 30 or 40 in a bad one.

At the end of 1999, Conway was diagnosed with stomach cancer. In the following years, he had chemotherapy and radiation therapy, and his involvement with the business ceased or diminished; the evidence varies. At trial, Piedra testified that he handled things after Conway's diagnosis.

Titan's taxi franchise was due to expire in December 2000. In June, Titan applied for a renewal of its taxi franchise. (Conway testified that he believed that with a new franchise, the business could be sold or turned around.) In December, the application was denied. Titan filed suit, but was unsuccessful, and Piedra and another employee began to shut the business down.

On October 12, 2001, the City filed an amended complaint in the Garcia action, adding Titan as a defendant. Titan answered. The following year, in September 2002,

the City filed a second amended complaint, naming Conway on an alter ego theory. The City also propounded discovery, which, according to a declaration filed by the City's counsel in the Garcia action, was intended to trace Valley Cab's assets.

Neither Titan nor Conway answered the second amended complaint or responded to requests for admission. Matters were deemed admitted,[3] and the trial court found that Valley Cab had a continuing pattern of avoiding service. On May 8, 2003, a default judgment in the amount of $78,124 was entered against Titan. A default judgment was entered against Conway, too, but in June 2003, he successfully moved to vacate the default. The parties agree that he was later dismissed from the action.

The City presented Conway's and Piedra's deposition testimony that for about three months after Titan lost the taxi franchise (the evidence was not more specific than that as to time), Titan attempted to run a car service, and that after Titan's car service failed, Piedra started a car service of his own, for which he took no assets from Titan. This, too, was short-lived. Conway testified that the dba of Titan's car service was "Valley Transportation," but he was also questioned about car services called "Valley Car," "West Valley Transportation," and "East Valley Transportation," and it is not entirely clear which of these was Titan's attempt at a car service, and which was Piedra's. According to Piedra's deposition, read into the record by the City, Titan paid Valley Transportation's bills by "changing the name on the account."

The City presented evidence concerning the disposition of Titan's assets after it could no longer operate a taxi business: in 2001 and the early months of 2002, Piedra and another employee sold the cabs, office equipment, and so on, paid the creditors and any claims, and shut down the business. Through the deposition testimony of Conway

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[3] We need not detail those matters. They were admitted for purposes of the Garcia action only, and cannot "be used in any manner against that party in any other proceeding." (Code Civ. Proc., § 2033.410.)

and Piedra, the City presented evidence that the cabs, office equipment, etc., were worth very little. Their testimony at trial was similar.

The City also presented evidence concerning two accounts Titan had at a brokerage firm, JB Oxford. One of those accounts constituted the mandatory faithful performance bond in favor of the City. On March 8, 2001, after the City released the bond, JB Oxford issued a $100,000 cashier's check to Titan, closing the account. The check was deposited into a Titan bank account. The other JB Oxford account was for Titan's self-insurance trust, also mandated by the City. On March 6, 2001, with the consent of the City's Department of Transportation, JB Oxford issued a check to Titan for $633,967, the balance in that account. This check, too, was deposited into a Titan account. Piedra's deposition testimony was that Titan had accounts at Wells Fargo, Bank of America, and California Federal Bank.

The City entered Ballenger's draft report into evidence. (There was no final report.) This report states that the JB Oxford checks represented fraudulent transfers to Conway and other insiders. However, in his testimony and on cross-examination, Ballenger testified that the report was written in anticipation of receiving bank records which showed transfers to Conway, and that in the absence of those records, nothing about either JB Oxford check indicated fraudulent transfer. Ballenger also testified that the report's reference to fraud was partly based on his belief that in 2000, Titan was insolvent, a belief he no longer held, and his belief that where a company is insolvent, payment to insiders is an improper preference under bankruptcy law.

In their depositions and at trial, Conway and Piedra testified that the proceeds of the JB Oxford accounts and all sums realized from the sale of the other assets were deposited into Titan's general account and used to pay for general operations and to pay accident claims and creditors.

Also after Titan lost the taxi franchise, Conway became 25 percent shareholder in a new corporation, West River. The City presented Piedra's deposition testimony that he

purchased a 25 percent share in West River for "a couple hundred thousand dollars," by paying Conway's bills over a period of years.

Valley Cab operated from premises on Aetna Street. The City presented Titan's application for renewal of its franchise, which stated that it "owned its own facilities." Piedra's testimony at trial was that the franchise application was false in this and other respects, and the City also presented Titan's 1999 and 2000 balance sheets, which do not show the Aetna property as a Titan asset; Conway's deposition to the effect that the Aetna property was owned by his wife and had "never been part of the corporation;" and other testimony, in Conway's 2006 deposition, that the Aetna property had by then been transferred to West River.

After it lost the taxi franchise, Titan disposed of Valley Cab's records. Piedra's deposition testimony was that the records were stored at Valley Cab for about six months, then were moved to a storage area in Van Nuys, and were discarded at some point. He did not remember when. At trial, he testified that there were 500 boxes of records and that they were moved from the premises because a new tenant took possession. He also testified that at the time he threw records away, the City had not made any claim against Titan in the Garcia case.

Conway testified that after his cancer diagnosis, in 2000 or 2001, he gave some records to Mike Itevi, a potential buyer. At trial, he testified that those records were the general ledgers, not the records Piedra later stored.

At trial, Piedra testified that he never transferred any money from Titan's accounts to either his personal account or Conway's, or to other companies in which he or Conway had an interest. Conway's testimony was the same.

Trial court findings

The principle relevant finding was that the City "strongly argues that the drafts returned from the brokerage accounts totaled more than $733,000.00, yet Defendants fail to offer an adequate or credible account of when and to whom this money was distributed. The Court agrees with Plaintiff that the evidence establishes a strong

inference that a substantial portion of the $733,000.00 was subject to fraudulent transfer and the court so finds."

The court also summarized the evidence concerning the JB Oxford accounts, and found that the funds were distributed with the City's knowledge. The court then noted the evidence concerning the number of cabs Titan owned, and that: "Plaintiff's case against Defendants consists essentially of circumstantial evidence, comprising the fact that Defendants presented no records, failed to properly dissolve pursuant to the Corporation Code, Defendants claim to have no remaining records of Valley Cab, offered conflicting explanations as to what happened to the Valley Cab records, Defendants could not recall the name of any other creditors, Defendants stopped defending [the Garcia case], and significant memory lapses of Defendants Conway and Piedra. Although Plaintiff's evidence substantially impaired the credibility of Defendants Conway and Piedra, Plaintiff offered little other testimony to establish value of the remaining assets. This lack of evidence from Plaintiff is particularly troubling since Plaintiff had the vehicle identification numbers of each of these vehicles together with Inspection Reports which included odometer mileage readings. Plaintiff could have easily called a witness to testify to value of these vehicles, which causes the court to accept Defendant's testimony despite their impaired credibility."

Much of the rest of the statement of decision concerns the statute of limitations, which is not at issue here. It is relevant to note that in rejecting the City's contention that the fraudulent transfers occurred after May of 2002,[4] the court found that "based upon the above evidence, including the loss of the Valley Cab's franchise in December of 2000, changing names on Valley Cab bank accounts, that Defendant operated other businesses at the Valley Cab location during 2001 through early 2002 the Court finds that the

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[4] Under Civil Code section 3439.90, the City had four years from the transfer to bring an action for fraudulent transfer, but the trial court found that the statute was tolled until judgment was entered against Titan in the Garcia case. (*Cortez v. Vogt* (1997) 52 Cal.App.4th 917.)

fraudulent transfers . . . began and were substantially completed at least before May of 2002. Additionally, the bulk of these transferred assets consisting of the liquidated brokerage accounts, were transferred or diverted from Valley Cab at least before May of 2002."

The court entered judgment[5] against Conway and Piedra jointly and severally, in the amount of $73,214, representing the damage to City property, minus Garcia's $5,000 payment, with interest from the date of the underlying judgment.

Discussion

Civil Code sections 3439.04, part of the Uniform Fraudulent Transfer Act, provides that "(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation as follows: (1) With actual intent to hinder, delay, or defraud any creditor of the debtor. (2) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor either: (A) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction. (B) Intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due." A creditor's remedies include avoidance of the transfer. (Civ. Code, § 3439.07, subd. (a)(1).)

The City proceeded under two theories, bringing a cause of action under section Civil Code section 3439.04, subdivision (a)(1), transfer with actual intent to defraud, and a cause of action under section 3439.04, subdivision (a)(2), alleging that Titan made the transfers without receiving reasonably equivalent value. Conway and Piedra argue that

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[5] In addition to two causes of action under Civil Code section 3439, the complaint brought causes of action for conspiracy and one titled "equitable trust fund theory." The trial court dismissed the causes of action, finding that neither was a cause of action, a finding which the City has not appealed.

the City did not carry its burden of proof on either theory, because it did not prove that any Titan asset was transferred to either Conway or Piedra. We agree.

"In determining whether a judgment is supported by substantial evidence, we may not confine our consideration to isolated bits of evidence, but must view the whole record in a light most favorable to the judgment, resolving all evidentiary conflicts and drawing all reasonable inferences in favor of the decision of the trial court. (*People v. Johnson* (1980) 26 Cal.3d 557, 576-578.)" (*Beck Development Co. v. Southern Pacific Transportation Co.* (1996) 44 Cal.App.4th 1160, 1203.)

We begin with the City's many arguments concerning the Aetna property, which is the City's focus on appeal, though not in the trial court. As the City argues, there was evidence that at some point after Titan lost the taxi franchise, the Aetna property was transferred to West River, to the benefit of both Conway and Piedra,[6] but that is irrelevant, because the City did not prove that Titan owned the Aetna property. That is, the City presented some evidence (Titan's franchise application) that Titan owned the property, but also presented evidence (Conway's testimony and the balance sheets) that it did not own the property. While we indulge all legitimate inferences in favor of the judgment, we do not see that we can pick and choose between the contradictory evidence

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[6] Piedra testified that he got the money to purchase a share of West River "from the business I was running." When asked "Valley Transportation?" he answered "yeah." He then testified that he was still paying the debt, that the checks were written on a Valley Transportation account, which was "my company," and "the company [he was] operating now." At trial, the defense objected to this testimony on relevance grounds. The City argued that the evidence was relevant to show "knowledge of how to transact business without a paper trail," and "to show the relationship that they have between each other." We thus cannot agree with the City that Piedra's testimony established that Titan dba Valley Transportation purchased a share of West River for Piedra. The testimony was not offered for that purpose, and is sufficiently confused (how could Piedra still be paying bills from a company that lasted only a few months?) that we do not believe that it constitutes proof of the fact.

presented by the party which has the burden of proof. This is especially true where the fact to be proven -- ownership of real property -- is a matter of public record.

"In a civil case the party with the burden of proof must convince the trier of fact that its version of a fact is more likely than not the true version. Stated another way, it requires the burdened party 'to convince the trier of fact that the existence of a particular fact is more probable than its nonexistence-a degree of proof usually described as proof by a preponderance of the evidence.' (Cal. Law Revision Com. com., 29B pt. 1 West's Ann. Evid. Code (1995) § 500, p. 553.)" (*Beck, supra,* 44 Cal.App.4th at p. 1205.) A party with the burden of proof does not carry that burden by presenting contradictory "versions of a fact."

Because the City did not prove that Titan owned the Aetna property, nothing about that property, or its transfer to West River or its use by Piedra, can constitute substantial evidence for the judgment here.

We note, too, that while the City refers to transfers of funds from Valley Cab to Titan, or from Titan to Valley Transportation, those are legal impossibilities. Valley Cab and Valley Transportation were Titan's dbas.

The City did prove that Titan had assets, the funds in the JB Oxford accounts and the money realized when the cars and equipment were sold, although the only evidence on the value of the cars and so on was that they were worth very little. However, the City did not present evidence that any of that money went to either Conway or Piedra. Instead, the City presented evidence, through Conway's and Piedra's depositions, that the money was used to pay Titan's bills. The City's own expert supported appellants' testimony that all assets went to pay creditors, with his testimony that at the relevant time period, Titan's assets equaled its liabilities.

The City argues, however, that there is circumstantial evidence which proves a fraudulent transfer to Conway and Piedra.[7] In support of this argument, the City cites the

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[7] The City is never more specific, and never, for instance, suggests how much either appellant might have gotten.

facts that Titan defaulted in the Garcia action, failed to formally dissolve, and, most notably, the fact Titan discarded its records.

We can see nothing in Titan's failure to dissolve which could logically lead to any conclusion about transfers to either Conway or Piedra. We say the same about the default. Titan did not stop defending until fall of 2002, well after the trial court concluded that it had completely disposed of its assets.

Now, as to the records. On this point, the City seeks to reverse the burden of proof by arguing that Conway and Piedra failed to present bank records which would have shown how Titan's funds were disbursed. In legal support, the City cites *Whitehouse v. Six Corp.* (1995) 40 Cal.App.4th 527, and also argues that destruction of records can constitute spoliation and lead to discovery sanctions, including a shift in the burden of proof. (*Williams v. Russ* (2008) 167 Cal.App.4th 1215.)

Whitehouse does not assist the City. That case held that "the creditor has the burden of proof to establish a fraudulent transfer. [Citation.] If the creditor shows that a conveyance made by a debtor is presumptively fraudulent because it has been made without fair consideration, the burden shifts to the party defending the transfer." (*Whitehouse v. Six Corp., supra,* 40 Cal.App.4th at p. 534.) The City did not prove a transfer, or a presumptively fraudulent transfer, and cannot take advantage of this rule.

Nor is the City assisted by its theory that the burden of proof is reversed due to spoliation, a theory which it did not advance in the trial court. "On rare occasions, the courts have altered the normal allocation of the burden of proof. [Citation.] The shift in the burden of proof from the plaintiff to the defendant rests on a policy judgment that there is a substantial probability the defendant has engaged in wrongdoing and the defendant's wrongdoing makes it practically impossible for the plaintiff to prove the wrongdoing. [Citation.] Thus, the normal allocation of the burden of proof has been shifted in spoliation of evidence cases [citation], negligence per se actions [citation], and product liability cases based on design defect [citation]. Even in these cases, however, the plaintiff has the burden of producing some evidence before the burden of proof is

shifted to the defendant. In spoliation of evidence cases, for example, the plaintiff must produce evidence that the defendant failed to preserve the evidence and establish a substantial probability of causation before the burden of proof shifts to the defendant to prove the failure to preserve the evidence did not cause damage to the plaintiff." (*National Council Against Health Fraud, Inc. v. King Bio Pharmaceuticals, Inc.* (2003) 107 Cal.App.4th 1336, 1346-1347, fns. omitted.)

Here, the City did not show that the destruction of the records (even if it was wrongdoing) made it "practically impossible" for it to prove its case. As appellants argue, the City itself could have presented the bank records it now faults appellants for failing to produce.

In its ruling on laches, the court found that "it is clear beyond a reasonable doubt Plaintiff knew the fraudulent transfers had already occurred or the Defendants were actively concealing assets in October of 2002. In fact, Plaintiff had knowledge of the $733,000 of assets that had been returned to Defendants in 2001. This information could reasonably have led Plaintiff to Defendants' corporate accounts at Wells Fargo as early as October of 2002 . . . ." The court found that laches and other equitable defenses do not apply, and we do not review that ruling here, but we do say that if the City waits almost two years to sue a corporation over a traffic accident, during which time (as the City knows) the corporation loses its ability to do business, then waits an additional four years to sue for fraudulent transfer, it cannot rely for its case in chief on an inference that the corporation's perfectly natural failure to preserve its records in the meantime means that fraudulent transfers took place.

At least as to Conway, the judgment must fail for another reason, which is that Titan owed him over $900,000. Even if there was a transfer of funds to him, "A transfer or an obligation is not voidable under paragraph (1) of subdivision (a) of Section 3439.04, against a person who took in good faith and for a reasonably equivalent value . . . ." (Civ. Code, § 3439.08, subd. (a).) Further, "A debtor may pay one creditor in preference to another, or may give to one creditor security for the payment of his

demand in preference to another." (Civ. Code, § 3432.) A transfer of all of the funds from the JB Oxford accounts and all the sums realized from the sale of the other assets, to Conway, would have been repayment of that loan, and not a fraudulent transfer.

The City argues that the transfer was nonetheless fraudulent, because it was made with the intent to defraud creditors, citing *Kemp v. Lynch* (1937) 8 Cal.2d 457. That case held only that "if a transfer while appearing to be a lawful preference is made with actual fraudulent intent that it shall not pay the creditor or give him further security, but with the understanding that it shall be a mere simulated transfer, the grantor retaining the full beneficial interest, such fraudulent intent will vitiate the transfer." (*Id.* at pp. 460-461.) Here, there was no evidence of actual fraudulent intent, or a "mere simulated transfer." The applicable rule is that payment of a debt cannot be deemed "an act to hinder, delay, and defraud creditors," even if the transfer is to an insider, and even if the transfer will prevent another creditor from collecting on his debt. (*Wyzard v. Goller* (1994) 23 Cal.App.4th 1183, 1191.)

Nor is the City's position supported by *Commons v. Schine* (1973) 35 Cal.App.3d 141, 144. In that case, the insider, Schine, totally dominated two corporations, one of which was bankrupt. He arranged to have the bankrupt corporation sell a portion of its property, then used the proceeds to repay loans made to it by the second corporation. As a result, Schine and the second corporation received payment in a greater percentage than the other general creditors of the bankrupt, on whose behalf the plaintiff sued. The court held that Civil Code section 3432 did not protect Schine: "One who dominates and controls an insolvent corporation may not, however, assert the general immunity of creditor preferences from attack. He may not use his power to secure for himself an advantage over other creditors of the corporation." Instead, Schine, who controlled the bankrupt corporation, occupied a fiduciary relationship to that corporation's creditors and was liable to those creditors for preferences taken for his benefit at their detriment. Here, Titan was not insolvent, let alone bankrupt, and the City did not sue on behalf of all

creditors or for breach of fiduciary duty. Instead, it sued under Civil Code section 3439.04, which allows transfers for value.

Finally, the City argues that Conway may not assert that any transfer to him was a repayment of a loan because both Piedra and Conway testified that the loans were not repaid and because this is a new theory on appeal. We see no barrier to Conway's assertion of this theory. In the trial court, appellants contended, and testified, that Conway received no transfer from Titan, and that the loans were not repaid. That is not inconsistent with the legal argument that, if Conway had received a transfer, it would as a legal matter constitute repayment of the loans.

The City also contends that it may recover from Conway on the theory that Titan was his alter ego. Aside from a few perfunctory references to alter ego in the complaint, the City did not proceed on those grounds in the trial court, let alone recover on those grounds. The issue was not litigated below, and we could not affirm on that basis.

Disposition

The judgment is reversed. Appellants to recover costs on appeal.

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

ARMSTRONG, Acting P. J.

I concur:

MOSK, J.

I respectfully dissent. I would affirm the judgment as there is substantial evidence of constructive fraud present when the transfers of the assets of Delaware Titan Capital Corporation occurred. (Civ. Code, § 3439.04, subds. (a)-(b).) The trial court was free to disbelieve the reasons given for the transfers. (*S. E. Slade Lumber Co. v. Derby* (1916) 31 Cal.App. 155, 160.)

TURNER, P. J.