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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

PHILLIP DODGE et al.,

Plaintiffs and Respondents,

v.

DOLLARSTORE, INC., et al.,

Defendants and Appellants.

G045064

(Super. Ct. No. 30-2008-00102967)

O P I N I O N

Appeal from a postjudgment order of the Superior Court of Orange County, Sherri Honer, Temporary Judge. (Pursuant to Cal. Const., art. VI, § 21.) Reversed and remanded.

Haight Brown & Bonesteel and Rita Gunasekaran for Defendants and Appellants.

The Chugh Firm and Paul S. Saghera for Plaintiffs and Respondents.

Defendants¹ appeal from a postjudgment order awarding attorney fees to plaintiffs.² But the court awarded those fees pursuant to an indemnification clause that does not provide for recovery of attorney fees in an action between the parties. The order is reversed.

FACTS

We addressed the underlying facts in *Dodge v. Dollarstore* (May 25, 2012, G044377) [nonpub. opn.] (*Dodge*). “Rakesh ‘Rex’ Mehta (Mehta) founded Dollarstore, Inc. (Dollarstore), and other entities to sell discount merchandise.” (*Dodge, supra*, G044377.) Plaintiffs provided money to Dollarstore and, in exchange, received convertible promissory notes, providing for the repayment plus interest or (upon a “Mandatory Conversion Event”) the issuance of Dollarstore shares. The parties also entered into a “LOAN AND SECURITY AGREEMENT” (Agreement). (*Dodge, supra*, G044377.) This Agreement contained a section entitled “Remedies; Limitation,” which provided that each “[plaintiff’s] sole remedy for a default by [Dollarstore] hereunder or under the Note shall be the right to convert the outstanding principal balance under the Note into shares of [Dollarstore’s] common stock . . . at a conversion price of \$0.25 per share.” The notes matured in 2005. Dollarstore neither repaid the loans nor issued shares to plaintiffs. (*Dodge, supra*, G044377.)

Plaintiffs filed suit against defendants in 2008 for breach of contract, common counts, and other causes of action. The court found defendants had breached

¹ The defendants at trial were Dollarstore, Inc.; Dollarstore Corporation, Dollarstore International, Inc.; Dollarstore.com Inc.; My Dollarstore Franchising, Inc.; Rex Mehta, aka Rakesh Mehta; Rishi Mehta; and Reeta Mehta.

² The plaintiffs at trial were Phillip Dodge; Raghav Sood aka Raj Sood; Nelson Brewart; Martha Brewart; Jeff Wilhelm; Susan Wilhelm; and Sukhdev Sharma.

their agreements, and the remedies-limiting provision of the Agreement was unconscionable. It awarded plaintiffs over \$620,000. We affirmed, holding that even if the remedies-limiting provision of the Agreement was enforceable, plaintiffs would still be entitled to recovery since they were not issued stock warrants per the Agreement. (*Dodge, supra*, G044377.)

Relying on a provision of the Agreement, plaintiffs moved to recover their attorney fees as the prevailing party. The relevant provision provides: “Indemnification. Lender recognizes that the offer and sale of Securities by Borrower to Lender were and will be based upon the representations, warranties, acknowledgements and agreements of Lender contained in this Agreement and hereby agrees to defend and indemnify the Borrower . . . with respect to the sale of the Securities, and to hold each such person or entity harmless from and against all losses, liabilities, costs, or expenses (including reasonable attorneys’ fees) arising by reason of or in connection with any misrepresentation or any breach of such warranty by Lender, or arising as a result of the sale or distribution of the Securities by the undersigned in violation of the Securities Act, or any applicable state securities laws, *or Lender’s failure to fulfill any of Lender’s covenants or agreements set forth herein.*” (Italics added.)

At the hearing, the court issued a tentative ruling for defendants. It reasoned the Agreement contained a simple indemnification provision and not an “embedded” prevailing party attorney fee clause. After additional briefing, the court issued a minute order for plaintiffs. It found the indemnification provision did incorporate an attorney fee clause, which was severable from the unconscionable remedy limitation. The court awarded over \$450,000 in attorney fees to plaintiffs.³

³ The court denied the motion with prejudice as to Dodge and Sood because no evidence showed they executed any Agreement. They did not cross-appeal from the denial of attorney fees.

DISCUSSION

Defendants make three contentions on appeal: (1) the purported attorney fees clause is really an indemnification provision; (2) the clause is unenforceable because the Agreement containing it was found unconscionable; and (3) this is not an action “on the contract” making the provision reciprocal. We agree the Agreement’s indemnification provision does not provide for recovery of attorney fees in a dispute between the parties. Thus, we need not address the last two contentions.

Reversing field, however, defendants also contend it is they who are entitled to an award of fees under the very same indemnity clause. We reject that contention as well.

The Indemnification Provision Is Not an Attorney Fee Clause

“Unless authorized by either statute or agreement, attorney’s fees ordinarily are not recoverable as costs.” (*Reynolds Metals Co. v. Alperson* (1979) 25 Cal.3d 124, 127.) Here, plaintiffs assert the Agreement’s “Indemnification” clause would have allowed defendants to recover their attorney fees had they prevailed, and, pursuant to Civil Code section 1717, plaintiffs therefore have the reciprocal right to recover their attorney fees as the prevailing party on the contract.⁴ Thus the underlying issue here is whether the Agreement’s “Indemnification” clause provides for the recovery of defendants’ attorney fees had they prevailed in defending plaintiffs’ action on the contract.

Indemnity agreements are construed under the same rules that govern the interpretation of other contracts. (*Myers Building Industries, Ltd. v. Interface Technology, Inc.* (1993) 13 Cal.App.4th 949, 969 (*Myers*.) Accordingly, the contract

⁴ All further statutory references are to the Civil Code.

must be interpreted to “give effect to the mutual intention of the parties.” (§ 1636.) The intention of the parties is to be ascertained from the “clear and explicit” contract language. (§ 1638.) “The words of a contract are to be understood in their ordinary and popular sense.” (§ 1644.) Determining whether a contract provides for the recovery of attorney fees is a question of law, and therefore is subject to our de novo review.

(Building Maintenance Service Co. v. AIL Systems, Inc. (1997) 55 Cal.App.4th 1014, 1021 (BMS).)

Ordinarily, an indemnification provision allows one party to recover costs incurred defending actions by third parties, not attorney fees incurred in an action between the parties to the contract. (See *BMS, supra*, 55 Cal.App.4th at p. 1030.) “[A]n indemnity clause . . . generally obligates the indemnitor to reimburse the indemnitee for any damages the indemnitee becomes obligated to pay third persons. [Citation.]

Indemnification agreements ordinarily relate to third party claims.” (*Myers, supra*, 13 Cal.App.4th at p. 969 [holding indemnification clause did not support award of attorney fees to prevailing party in action between parties to the contract].)

Courts look to several indicators to distinguish indemnification provisions from provisions for the award of attorney fees incurred in litigation between the parties to the contract. The key indicator is an express reference to indemnification. “A clause which contains the words ‘indemnify’ and ‘hold harmless’ is an indemnity clause” (*Myers, supra*, 13 Cal.App.4th at p. 969; accord *BMS, supra*, 55 Cal.App.4th at p. 1029.)

The courts also examine the context in which the language appears. Generally, if the subject matter heading of the contract incorporates a word like “indemnify,” and the surrounding provisions describe third party liability, the clause will be construed as a standard indemnification provision. (*BMS*, at p. 1030; *Myers*, at p. 970.) The court will not infer that the parties intended an indemnification provision to cover attorney fees between the parties if the provision ““does not specifically provide for attorney’s fees *in an action on the contract*” (*Myers*, at p. 970.)

For example, language stating, “Seller . . . agrees to indemnify and save buyer . . . harmless from any and all losses . . . including . . . reasonable attorney’s fees . . . arising from any cause or for any reason whatsoever,” does not separately provide for attorney fees. (*BMS, supra*, 55 Cal.App.4th at pp. 1022, 1030.) The *BMS* court concluded that “there is no language . . . which reasonably can be interpreted as addressing the issue of an action between the parties on a contract.” (*Id.* at p. 1030.) The *BMS* court considered the heading (titled “Indemnification”) and effect of surrounding clauses, in which BMS promised to “indemnify and save Buyer . . . harmless from any and all losses” (*id.* at p. 1022) in determining that one could not make a reasonable inference that the parties had negotiated to address an action between themselves (*id.* at p. 1030). “[G]iving consideration to the ordinary meaning of the words used [citation] . . . [citation], we conclude that the provision was intended to deal with only third party claims.” (*Ibid.*)

Similarly, an indemnification clause titled “Contractor’s Liability” in which one party promised to “indemnify” the other from “any, all, and every claim” which arises out of “the performance of the contract,” was intended to deal with only third party claims. (*Myers, supra*, 13 Cal.App.4th at p. 974.) The *Myers* court held that considering “the ordinary meaning of the words” (*ibid.*) “indemnify” and “hold free and harmless” (*id.* at p. 965), as well as “the subject matter heading and giving effect to the entire provision,” the contract could not be construed as separately providing for attorney fees in an action between the parties (*id.* at p. 974).

Here, the Agreement’s indemnification provision is just that — an indemnification provision. The purported attorney fee clause lies within a paragraph entitled “Indemnification.” It obligates plaintiffs to “defend and indemnify . . . and to hold [defendants] harmless from and against all losses” This is a “standard third party claims indemnification clause.” (*Myers, supra*, 13 Cal.App.4th at p. 973.) Plaintiffs also agree to indemnify defendants from all claims arising out of “Lender’s

failure to fulfill any of Lender's covenants or agreements set forth herein." (Italics added.) When taken in context, the "ordinary . . . sense" (§ 1644) of this language merely extends plaintiffs' duty to indemnify Dollarstore against third party claims to those based on plaintiffs' breach. And since the contract does not "'specifically provide'" otherwise, we conclude as a matter of law that the contract does not contain a prevailing party attorney fee provision. (*Myers, supra*, 13 Cal.App.4th at p. 970.)

Plaintiff relies on two cases that are distinguishable. In *Baldwin Builders v. Coast Plastering Corp.* (2005) 125 Cal.App.4th 1339, the court awarded attorney fees under an agreement which contained an *express* attorney fee clause, which obligated one party to pay another "'all costs, including attorney's fees, incurred in enforcing this indemnity agreement.'" (*Id.* at p. 1345.) And in *Continental Heller Corp. v. Amtech Mechanical Services, Inc.* (1997) 53 Cal.App.4th 500 (*Continental Heller*), a contract provision had to be construed as an attorney fee clause to be more than surplusage. In that case, section 11 of the contract set forth seven subparagraphs, with a standard indemnity clause in subparagraph (b). (*Id.* at p. 508.) But the contract also contained "an additional provision on attorney fees" "[f]ollowing the last subparagraph" of section 11. (*Ibid.*) This separate clause provided: "'And the Subcontractor shall indemnify the Contractor, and save it harmless from any and all loss . . . and attorney's fees suffered or incurred on account of any breach of the aforesaid obligations and covenants, and any other provision or covenant of this Subcontract.'" (*Id.* at pp. 508-509.) The *Continental Heller* court held: "It is clear this concluding paragraph is not referring to indemnity for attorney fees incurred in defending actions brought against Continental. That indemnity is covered in subparagraph (b) of the section. Rather, the quoted language is intended to entitle Continental to attorney fees in any action it brings against Amtech for breach of any provision of the contract including, but not limited to, breach of the indemnity provisions of subparagraph (b)." (*Id.* at p. 509.)

The contract language here stands in stark contrast to these cases. The indemnification provision does not refer to fees “*incurred in enforcing [the] agreement*” between the parties. (*Baldwin, supra*, 125 Cal.App.4th at p. 1345.) Nor must it be construed as such in order to be meaningful. (*Cf. Continental Heller, supra*, 53 Cal.App.4th at p. 509.) Instead it extends the scope of the duty to reimburse costs incurred in defending against third party claims arising from conduct that breached the Agreement. It is an integral part of the indemnification provision.

Defendants Are Not Entitled to Recover Attorney Fees

Defendants contend they are entitled to attorney fees under the same indemnification clause on the ground that plaintiffs breached the Agreement by filing this lawsuit in violation of a provision of the Agreement whereby they arguably promised not to bring an action against Dollarstore unless Dollarstore was in an undismissed bankruptcy proceeding for at least 60 days. In other words, after making lengthy arguments that the indemnification provisions applied only to third party claims against Dollarstore, defendants now assert they are nevertheless entitled to treat the indemnification provision as a prevailing party attorney fee clause. Remarkably, the argument is made here on appeal, wholly unsupported by any trial court finding that plaintiffs breached the contract by filing this lawsuit. Even more remarkably, defendants assert they are entitled to reimbursement for their fees without ever having raised the request for attorney fees below. “As a general rule, ‘issues not raised in the trial court cannot be raised for the first time on appeal.’” (*Sea & Sage Audubon Society, Inc. v. Planning Com.* (1983) 34 Cal.3d 412, 417.) Defendants merely opposed plaintiffs’ motion below. They never asked the trial court to award them attorney fees. They filed no motion to recover attorney fees. They never gave the trial court an opportunity to consider whether they should recover their attorney fees, but now seek them ““for the

first time on appeal.”” (*Ibid.*) We are a court of review and decline to consider an issue never considered below.

In their reply brief, defendants argue for the first time on appeal they are entitled to attorney fees for defeating plaintiffs’ claim to attorney fees. Again, defendants have reversed positions by arguing, in effect, that the indemnity provision is actually a prevailing party attorney fee clause, thereby entitling them to an award of attorney fees under a (double) reciprocity theory. Defendants rely on the dubious proposition: “Where a party claims a contract allows fees and prevails, it gets fees. Where it claims a contract allows fees and loses, it must pay fees.” (*International Billing Services, Inc. v. Emigh* (2000) 84 Cal.App.4th 1175, 1190 (*International Billing*)).) But the California Supreme Court has never embraced so broad a rule. It is only when “a party litigant prevails in an action on a contract by establishing that the contract is invalid, inapplicable, unenforceable, or nonexistent,” the high court held, that “section 1717 permits that party’s recovery of attorney fees whenever the opposing parties would have been entitled to attorney fees under the contract if they had prevailed.” (*Santisas v. Goodin* (1998) 17 Cal.4th 599, 611.)

Fittingly, the Third District Court of Appeal that decided *International Billing* has purported to decline to follow it. That court criticized the “rule” upon which defendants rely. (*M. Perez Co., Inc. v. Base Camp Condominiums Assn. No. One* (2003) 111 Cal.App.4th 456, 466 (*Perez*)).) The *Perez* court noted the *International Billing* plaintiffs alleged the contract provided for the recovery of attorney fees — but then, after losing, they opposed the defendant’s attorney fee request by contending the contract had no attorney fee clause. (*Id.* at pp. 463-464.) The *Perez* court recognized *International Billing* made improper use of the judicial estoppel doctrine. (*Id.* at p. 469.) And it was only in dictum that *International Billing* enunciated the “rule” on which defendants now try to rely. (*Id.* at p. 464.)

Further, the *Perez* case has itself been criticized. In *Blickman Turkus, LP v. MF Downtown Sunnyvale, LLC* (2008) 162 Cal.App.4th 858, the Court of Appeal pointed out an inconsistency in the *Perez* court's reasoning. *Perez* first stated that "a prevailing party is entitled to attorney fees only if it can prove it would have been liable for attorney fees had the opponent prevailed." (*Perez, supra*, 111 Cal.App.4th at p. 467.) But it then "cast in doubt" the meaning of this formulation of the rule by concluding that the "rule of *International Billing* continued to apply where the losing party had attempted unsuccessfully to establish that the alleged contract included a fee provision." (*Blickman Turkus*, at p. 899.) The *Blickman Turkus* court concluded: "We believe the better rule is the one stated in [*Leach v. Home Savings & Loan Assn.* (1986) 185 Cal.App.3d 1295, 1307]: A party claiming [a reciprocal right to] fees under section 1717 must 'establish that the opposing party *actually* would have been entitled to receive them if he or she had been the prevailing party.'" (*Ibid.*) Under this formulation of the rule plaintiffs cannot recover their attorney fees under the indemnification provision. Defendants cannot either.

But we need not tarry long over the alternate formulations of the "correct" formulation of the rule. Defendants raised this argument for the first time in their reply brief. "Points raised for the first time in a reply brief will ordinarily not be considered, because such consideration would deprive the respondent of an opportunity to counter the argument." (*American Drug Stores, Inc. v. Stroh* (1992) 10 Cal.App.4th 1446, 1453.) Defendants have not shown good cause to depart from the usual rule.

DISPOSITION

The postjudgment order awarding attorney fees is reversed, and the matter is remanded to the court with directions to vacate its order and enter a new order denying plaintiffs' motion for attorney fees. Defendants are to recover their costs on appeal, but not their attorney fees.

IKOLA, J.

WE CONCUR:

RYLAARSDAM, ACTING P. J.

ARONSON, J.