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NOT TO BE PUBLISHED IN OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

WILLOWBROOK APARTMENTS, LLC, et al., Plaintiffs and Appellants, v. HIRSCHLER FLEISCHER, APC et al., Defendants and Respondents.	G051265, G051345, G051628 (Super. Ct. No. 30-2013-00623935) O P I N I O N

Appeal from a judgment of the Superior Court of Orange County, Thierry Patrick Colaw, Judge. Affirmed.

Catanzarite Law Corporation, Kenneth J. Catanzarite and Eric V. Anderton for Plaintiffs and Appellants.

Lester & Cantrell, Mark S. Lester, David Cantrell and Colin A. Northcutt for Defendant and Respondent Hirschler Fleischer.

Morgan, Lewis & Bockius, J. Warren Rissier and Jordan McCrary for Defendant and Respondent CBRE, Inc.

Cooley, Steven M. Strauss, M. Ray Hartman III, and Dennis C. Crovella for Defendants and Respondents Sovereign Capital Management Group, Inc., and IUC-SOV, LLC.

* * *

This appeal is déjà vu all over again. It is one of several cases presenting similar fact patterns, and in some cases, they are functionally identical. This is one of those cases. As to two of the defendants, it is functionally identical to a case we already decided, *WA Southwest 2, LLC v. First American Title Ins. Co.* (2015) 240 Cal.App.4th 148 (*WA Southwest*).

The plaintiffs invested in properties, and certain costs were allegedly concealed from them. Those costs, however, were disclosed in the private placement memorandums (PPMs) that plaintiffs received prior to investing. Plaintiffs contend the PPMs contain confusing and contradictory statements concerning those costs. But even if that were enough to state a claim, plaintiffs face a more acute problem — they filed their lawsuit after the statute of limitations had expired. To get around that, they rely on the discovery rule. But even if the PPMs were unclear, the allegedly concealed costs were sufficiently disclosed to put plaintiffs on notice of their claim at the outset of their investment. Thus their claims are time barred. A law firm and real estate broker involved in the transaction demurred on this ground, and we affirm that ruling.

The one difference between this case and *WA Southwest* is the presence of respondents Sovereign Capital Management Group, Inc. (Sovereign Capital), and IUC-SOV, LLC ("IUC-SOV"), both of which are allegedly successors in interest to the parties that organized and promoted the investment opportunity. They demurred on the ground that the complaint inadequately alleges successor-in-interest liability. The trial court agreed, as do we. Accordingly, we affirm.

FACTS

The following factual allegations are derived from the fourth amended complaint. Because we have described the allegations in detail multiple times before, we present a simplified version of the 116-page fourth amended complaint. We will address the specific allegations concerning successor liability in the discussion section.

This lawsuit arises out of investments in four properties. In each case, plaintiffs received tenant-in-common (TIC) interests. The same defendants were involved in all four properties. Plaintiffs invested $1,245,020 in a property located in Pennsylvania; $776,224 in a property located in Illinois; $1,118,812.50 in a property located in Florida, and $795,000 in a property located in Georgia. The promoters had acquired the property, then sold tenant-in-common interests, structured as securities, to various investors, including plaintiffs. The purpose of the investment, in addition to profit, was to acquire like-kind property that enabled plaintiffs to defer the 15 percent capital gains tax on the prior sale of real estate under Internal Revenue Code section 1031 (1031 exchange).

Because one purpose of the investment was to defer the 15 percent capital gains tax, it was important to plaintiffs that the costs associated with the TIC investment be less than 15 percent. Plaintiffs allege they were told the costs between all four investments would be approximately 9.4 percent.[1] They would not have invested had the costs exceeded 15 percent.

Unbeknown to plaintiffs, defendants were conspiring to hide certain costs that, in fact, did raise costs above 15 percent. In particular, defendants and the original sellers agreed on a price at which the property could be acquired, but then marked up the purchase price in an amount sufficient to pay a commission to one of the promoter defendants (we refer to this as the "markup"). They then described the fee as being paid by the *sellers*, when in fact, for all practical purposes, it was the buyers, including plaintiffs, who were paying that fee by virtue of the markup. These markups amounted to $4 million for the Pennsylvania property, $3.5 million for the Illinois property, $1.6 million for the Florida property, and $400,000 for the Georgia property. The effect was to increase the "Sales Load" in each case, meaning the costs associated with organizing and marketing the TIC investments, exclusive of standard property acquisition costs such as loan points. The sales loads increased as follows: From 9 percent to 20.4 percent for the Pennsylvania property, from 9.7 percent to 21.7 percent for the Illinois property, from 9 percent to 15.6 percent for the Florida property, and from 9.7 percent to 15.9 percent for the Georgia property. In total, this raised the average sales load from 9.5 percent to 18.6 percent, which is greater than what plaintiffs would have paid in capital gains taxes.

The investments closed in 2006. Plaintiffs filed suit in July 2012, roughly six years later. Plaintiffs named 21 defendants in the fourth amended complaint. Most of the defendants are not parties to this appeal.

The respondents to this appeal are not the parties who were most directly involved in marketing and organizing the investment, who we refer to generally as the

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[1] In their briefs, plaintiffs clarify that it is the securitization and organizational costs that needed to be below 15 percent. Costs associated with standard real estate transactions would have been incurred whether or not plaintiffs performed a 1031 exchange.

"promoter defendants." Respondent CBRE, Inc. (CBRE), was the broker that represented the original sellers of the properties. Respondent Hirschler Fleischer, APC (Hirschler Fleischer), is the law firm that drafted an opinion letter supporting the 1031 exchange, which was included with the offering memoranda. Respondent IUC-SOV is an alleged successor in interest to one of the promoter defendants by virtue of purchasing shares in that company five years after the transaction at issue here took place. Plaintiffs allege IUC-SOV assumed any liability for the fraud. Respondent Sovereign Capital is a parent company of IUC-SOV, having formed IUC-SOV for purposes of acquiring an ownership stake in the promoter defendants.

The fourth amended complaint sets forth the following 16 causes of action: breach of fiduciary duty — real estate broker; legal malpractice; breach of fiduciary duty attorney; "breach of contract, statute, and fiduciary duties" (once against the escrow companies, and once against everyone else); constructive fraud; intentional misrepresentation; fraud by concealment; negligent misrepresentation; conversion; restitution and unjust enrichment; negligence; unfair business practices (Bus. & Prof. Code, § 17200 et seq.); accounting; breach of contract; and breach of the covenant of good faith and fair dealing.

The court sustained demurrers by each of the respondents, noting, with regard to CBRE and Hirschler Fleischer, "Plaintiffs have failed to state sufficient facts to state a claim in each of the above causes of action and each cause of action is barred by the statute of limitations applicable based on the facts alleged." The court sustained demurrers by Sovereign Capital and IUC-SOV on the ground they had not inherited the liability of the promoter defendants. The court also took judicial notice of the PPMs.

The PPMs, which plaintiffs acknowledge they received prior to closing the investment, contain disclosures about the precise costs plaintiffs claim were concealed. For example, the PPM associated with the Pennsylvania property states, "**Purchase Price Increase. The purchase price for the Property negotiated by the Manager and the**

seller has been increased by the approximately $4,000,000 real estate commission to be paid by the seller to the Property Manager, an Affiliate of the Manager, which increases the compensation payable to the Manager and its Affiliates in connection with this Offering. . . . While the real estate commission is being paid by the seller, the Company could have obtained a reduced purchase price if the commission was not paid. Since the purchase price for the Property was increased to include the additional commission, the value of the Property, and the related proceeds to be raised in this Offering, should be considered inflated by this additional cost."~**(1AA 278)**~

The same PPM also contains a chart setting forth the estimated use of proceeds. It contains the following information:[2]

	Percentage of Gross Proceeds
Gross Offering Proceeds	100.0%
Organization and Marketing	(2.50%)
Selling Commissions	(6.50%)
Marketing and Due Diligence	(2.50%)
Available for Investment	(88.50%)
Down Payment for Purchase of Real Estate	(79.52%)
Loan Fee and Costs	(2.73%)
Closing and Carrying Costs	(4.01%)
Reserve	(2.24%)
Proceeds Utilized	88.50%

[2] The actual table in the PPM contains additional information not relevant to this appeal. For the sake of clarity, we note that the percentages here are of the equity invested.

Offering and Organization Expenses and Fees	11.50%
Total Application	100.0%

In the PPM, most of the line items in this chart have footnotes that explain various facets of the line item. The "Down Payment for Purchase of Real Estate" line contains a footnote with another warning concerning the $4 million real estate commission: "The Seller will pay Triple Net Properties Realty, Inc., an Affiliate of the Manager, an approximately $4,000,000 real estate commission at settlement for arranging the purchase. The real estate commission will be paid by the Seller of the Property and will not be paid out of the proceeds of the Offering. While the commission is being paid by the Seller, a reduced purchase price could have been obtained if the commission was not paid. Therefore, the value of the Property and the related proceeds to be raised in this Offering should be considered increased by this additional cost." Similar statements and charts can be found in the PPMs for the other three properties.

On the other hand, elsewhere the PPM states, "The total aggregate amount of commissions and expense reimbursements . . . will not exceed 9% of the Gross Proceeds." The markup does not appear to have been accounted for either in the chart (with the exception of the footnote) or in the 9 percent limitation on commissions and expense reimbursements.

On appeal, plaintiffs have limited their assignment of error to "the claims for Breach of Fiduciary Duty of a Real Estate Broker, Legal Malpractice, Breach of Fiduciary Duty of an Attorney, Constructive Fraud, Intentional Misrepresentation, Fraud by Concealment, Negligent Misrepresentation, Restitution and Unjust Enrichment and Unfair Business Practices."

DISCUSSION

The Claims Against Hirschler Fleischer and CBRE are Time Barred

Plaintiffs contend that, by operation of the discovery rule, the statute of limitations began running when they consulted with counsel for a similarly situated plaintiff in a case brought by another investor in late 2011. On this issue, this case is functionally identical to *WA Southwest*, which we quote at length below. To the extent this case differs, we have bracketed the facts corresponding to the facts of the present case.

"The court sustained the demurrers at issue on statute of limitations grounds. Our de novo review of the orders 'is limited to issues which have been adequately raised and supported in [appellants' opening] brief.' [Citations.]

"Applicable California statutes of limitations in this case range from one to four years. [Citations.] . . . [Citations.] Plaintiffs' briefs do not identify the applicable statutes of limitations or contest the notion that the longest potentially applicable statute of limitations in this case is four years.

"Plaintiffs purchased their interests in the Property in [2006]. The initial complaint was not filed until [July] 2012. The only argument plaintiffs make on appeal is that the court should have applied the delayed discovery rule to postpone accrual of the statute of limitations. 'By their reliance on the "discovery rule," plaintiffs concede by implication that, without it, their claims are barred by one or more statutes of limitations.' [Citation.] Unless the discovery rule applies, the statute of limitations began running when plaintiffs made what they now deem to be unsuitable investments, paid what they now deem to be an unreasonable (and undisclosed) sales load, and had in their possession documents disclosing the downsides of the investment (e.g., the risks of the investment and the expenses beyond the acquisition price of the Property). . . .

"'An important exception to the general rule of accrual is the "discovery rule," which postpones accrual of a cause of action until the plaintiff discovers, or has reason to discover, the cause of action.' [Citation.] 'The discovery rule only delays accrual until the plaintiff has, or should have, inquiry notice of the cause of action.' [Citation.] A plaintiff relying on the discovery rule must plead '"(1) the time and manner of discovery *and* (2) the inability to have made earlier discovery despite reasonable diligence."' [Citation.] Plaintiffs have an obligation to plead facts demonstrating reasonable diligence. [Citation.]

"'Where a fiduciary obligation is present, the courts have recognized a postponement of the accrual of the cause of action until the beneficiary has knowledge or notice of the act constituting a breach of fidelity. [Citations.] The existence of a trust relationship limits the duty of inquiry. "Thus, when a potential plaintiff is in a fiduciary relationship with another individual, that plantiff's burden of discovery is reduced and he is entitled to rely on the statements and advice provided by the fiduciary."' [Citation.] But, even assuming for the sake of argument that each of the respondents had a fiduciary duty to plaintiffs, this does not mean that plaintiffs had no duty of inquiry if they were put on notice of a breach of such duty." (*WA Southwest, supra*, 240 Cal.App.4th at pp. 155-157.)

The discovery rule has no application here. The supposedly secret markups were explicitly disclosed in two different places in each of the PPMs. The two disclosures were obviously sufficient to put plaintiffs on notice of the markups. As we said in *WA Southwest*, "Reasonable diligence in such circumstances does not consist of ignoring a private placement memorandum received prior to making an investment." (*WA Southwest, supra*, 240 Cal.App.4th at p. 157.) And while we can understand some confusion resulting from the limitation on commissions and expenses to 9 percent of the gross proceeds, the fact remains that the commissions and expenses were accounted for apart from the markup, and the markup was separately disclosed. At minimum, these facts put plaintiff on notice that the markup was "inflating," to use the PPMs' term, the cost of the investment. We see no way for plaintiffs to amend the complaint to cure this deficiency. Accordingly, there was no error in sustaining the demurrers without leave to amend as to Hirschler Fleischer and CBRE.

Plaintiffs Inadequately Pleaded Successor-in-Interest Liability

Next, plaintiffs claim the court erred in sustaining the demurrer as to Sovereign Capital and IUC-SOV. The focus of the parties' briefing concerns whether the complaint adequately pleads successor liability.[3] To address this issue, we set forth a more detailed account of the facts surrounding the involvement of Sovereign Capital and IUC-SOV.

We begin by unpacking the parties we have generically referred to as the promoter defendants. In July 2006 plaintiffs were approached by Triple Net Properties, LLC (Triple Net), and related entities, which urged plaintiffs to invest in the TIC interests. Plaintiffs acquired the TIC interests in 2006. In 2007, Triple Net merged with Grubb & Ellis Corporation (Grubb & Ellis). Triple Net brought with it a property portfolio of 130 properties. In February 2011, Grubb & Ellis formed a wholly owned subsidiary — defendant Daymark Advisors — and transferred to it all of the Triple Net assets, including the TIC management contracts related to the properties at issue here.

In August 2011, Grubb & Ellis sold all of the stock of Daymark Advisors to respondent IUC-SOV. IUC-SOV had been formed the prior week as a joint venture by respondent Sovereign Group and another set of defendants for the purpose of acquiring the shares of Daymark Advisors. IUC-SOV assumed $10.7 million in liabilities that had

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[3] IUC-SOV and Sovereign Capital did not demur on statute of limitations grounds.

been listed on Grubb & Ellis's books as "inter-company loans."[4] In addition to the Daymark Advisors stock, Grubb & Ellis paid IUC-SOV $5 million.

Beyond these alleged facts, plaintiffs included pages and pages of speculative and conclusory statements, such as that everyone secretly knew Daymark Advisors had $100 million in unaccounted liabilities, and that all parties involved consummated this transaction for the sole purpose of mismanaging property, diluting investors, and generally acting in nefarious and dastardly ways. We disregard the speculation and conclusions and focus solely on the alleged facts.

The alleged facts do not provide a basis for successor liability. "[U]nder traditional rules of corporate successor liability an acquiring corporation does not assume an acquired corporation's liabilities when it purchases the acquired corporation's stock . . . ." (*Phillips v. Cooper Laboratories* (1989) 215 Cal.App.3d 1648, 1660.) That is precisely what happened here. The stock of Daymark Advisors was sold to IUC-SOV as part of a package deal in which IUC-SOV agreed to take on $10.7 million in liabilities in exchange for $5 million and control of the assets in the Daymark Advisors portfolio. The $10.7 million of liabilities were on Grubb & Ellis's books — *not* Daymark Advisors' books. Thus Daymark Advisors was sold with all of its assets and liabilities intact. Under these circumstances, IUC-SOV is merely a shareholder and is not saddled with successor liability. And Soveriegn Capital, as a partner in the IUC-SOV joint venture, is likewise free of successor liability.

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[4] Plaintiffs allege these liabilities were "attributed to" Daymark Advisors. It is unclear what this means or how it is to be reconciled with the liabilities being on Grubb & Ellis's books. This sort of contradiction is undoubtedly what led two different superior court judges to describe the complaint as "'nearly unintelligible.'"

The allegations that IUC-SOV, Sovereign Capital, and Daymark Advisors are alter egos of each other are rife with speculation and conclusions of fact and of law, and do not set forth allegations of fact that would demonstrate that an "inequitable result" would obtain if the alter ego doctrine were not applied. (See *Leek v. Cooper* (2011) 194 Cal.App.4th 399, 411.)

Accordingly, we affirm the trial court's ruling sustaining the demurrer as to IUC-SOV and Sovereign Group.

Finally, we find no abuse of discretion in the denial of leave to amend. As the court explained in its ruling, "as late as [the] ruling on the demurrers to the Third Amended Complaint the previous trial judge observed that the pleading was 'nearly unintelligible' and directed that the role/activity of each defendant must be explained in detail, alter-ego explained in detail, that 'transfer of assets' as distinguished from transfer of stock must be explained as well as facts supporting conclusions that an entity had 'ceased to exist' and that plaintiffs must separate 'investment fraud' from claims of property mismanagement." This was an accurate appraisal. Plaintiffs failed to cure the deficiencies. They are not entitled to yet another opportunity.

DISPOSITION

The judgment is affirmed. Respondents shall recover their costs incurred on appeal.[5]

IKOLA, J.

WE CONCUR:

O'LEARY, P. J.

FYBEL, J.

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[5] Sovereign Capital filed a motion in our court to take judicial notice of Securities and Exchange Commission Form 8-K, dated August 10, 2011, for Grubb & Ellis, as well as an exhibit to that filing, which is the stock purchase agreement pertaining to the sale of Daymark Advisors stock by Grubb & Ellis to IUC-SOV. Hirschler Fleischer and CBRE each filed a motion in our court to take judicial notice of the PPM. The trial court took notice of all three documents, and plaintiff does not oppose us taking judicial notice of the existence of these documents, but does oppose us noticing the truth of the statements in the documents. We grant each of the motions for judicial notice.