

FREEDOM FILMS, LLC, Plaintiff and Respondent,

v.

NU IMAGE, INC., et al., Defendants and Appellants.

Nos. B236216, B236765.

Court of Appeals of California, Second District, Division One.

Filed August 30, 2012.

Costa Abrams & Coate, Charles M. Coate, Darius Anthony Vosylius and Theresa E. Johnson for Defendants and Appellants.

Liner Grode Stein Yankelevitz Sunshine Regenstreif & Taylor, Edward A. Klein and Ashley R. Yeargan; Esner, Chang & Boyer and Stuart B. Esner for Plaintiff and Respondent.

ROTHSCHILD, J.

Freedom Films, LLC sued Nu Image, Inc. and M3 Media, Inc. for breach of contract, an accounting and fraud based on an agreement under which it contends that it was to receive a portion of gross proceeds from and other rights regarding a motion picture entitled *The Mechanic*. It later amended its complaint to add as doe defendants Sacred Productions, Inc., Sacred Productions, LLC and Millennium Films, Inc. The original defendants and the doe defendants each brought a motion to compel arbitration of the action. The trial court denied the motions on the ground that the parties had not entered into an agreement to arbitrate Freedom Films's rights as to *The Mechanic*. Both groups of defendants appealed the denial orders. We consolidated the appeals and now affirm the orders.

FACTUAL AND PROCEDURAL BACKGROUND

1. The Operative Complaint

On April 1, 2011, Freedom Films filed the operative first amended complaint against Nu Image and M3 Media, alleging causes of action for breach of contract, an accounting and fraud. According to the allegations, on or about February 14, 2006, Freedom Films entered into an agreement with Home of the Brave Productions, Inc., giving Freedom Films accounting and audit rights with respect to the motion picture *Home of the Brave*. Nu Image guaranteed the obligations to Freedom Films under the agreement and was the sales agent for the motion picture.

The operative complaint further alleged that, as sales agent, Nu Image entered into a distribution agreement with Metro-Goldwyn-Mayer Studios, Inc. (MGM) on May 17, 2006.

The distribution agreement contained a dispute resolution provision, requiring arbitration of a dispute if it could not first be resolved by the parties themselves and then by a mediator.^[1] Freedom Films claimed that MGM did not fulfill its obligations under the distribution agreement and thus filed and prosecuted an arbitration against MGM, in the name of Nu Image and Home of the Brave Productions, with the goal of securing Nu Image, Home of the Brave Productions and Freedom Films their respective benefits under the distribution agreement. The parties settled in early 2009.

In connection with the settlement, on January 23, 2009, Nu Image, Home of the Brave Productions and Freedom Films entered into a letter agreement, giving Freedom Films accounting and audit rights with respect to several to-be-produced motion pictures, including *The Mechanic*. According to the letter agreement, Freedom Films "will be entitled to the same accounting and audit rights in connection with the Settlement Pictures hereunder [including *The Mechanic*], as those accorded Nu Image pursuant to the MGM [distribution] [a]greement dated May 17, 2006 between MGM and Nu Image, Inc. for 'Home Of The Brave' . . . pursuant to paragraph 10 and the audit schedule attached" to the distribution agreement. In addition, "Nu Image will use its good faith efforts to cause [Freedom Films] to receive duplicate accountings directly from MGM." The letter agreement also provided that "Nu Image will use good faith efforts to cause [actor] Brian Presley to be cast in a lead role in 'The Mechanic' not less than [the] 3rd lead." The letter agreement did not contain an arbitration provision.

Also in connection with the settlement, on February 10, 2009, MGM, on the one hand, and Nu Image, Home of the Brave Productions and Freedom Films, on the other hand, entered into a "Confidential Settlement Agreement And General Release [('Settlement Agreement')]," which incorporated the dispute resolution provision in the distribution agreement.^[2] A separate "Term Sheet," also entered on February 10, 2009, between Nu Image and MGM listed the motion pictures encompassed by the settlement, including *The Mechanic*.

According to the operative complaint, Nu Image and M3 Media, the successor company to Home of the Brave Productions, "have failed and refused to comply with the[] terms and provisions" of the January 23, 2009 letter agreement. Specifically, Freedom Films alleged that Nu Image and M3 Media "have not paid to [Freedom Films] any portion of gross proceeds they derived from *The Mechanic*; . . . have not complied with the [letter] [a]greement's accounting and audit provisions; . . . did not use good faith efforts to cast Mr. Presley in *The Mechanic*. In fact, unbeknownst to [Freedom Films], from the outset [Nu Image and M3 Media] never intended to comply with their obligations under the [letter] [a]greement. [They] never intended to pay to [Freedom Films] any portion of gross proceeds from *The Mechanic* or provide complete and accurate financial records in compliance with the [letter] [a]greement's accounting and audit obligations. Moreover, [they] never intended to use good faith efforts to cast Mr. Presley in a lead role in *The Mechanic*—and engaged in conduct designed to deprive Mr. Presley from this significant acting opportunity from which [Freedom Films] would have derived value." Freedom Films sought compensatory and

punitive damages, as well as an accounting to determine the portion of gross proceeds from *The Mechanic* due to it under the letter agreement.

Freedom Films later amended the operative complaint to add as doe defendants Sacred Productions, Inc., Sacred Productions, LLC and Millennium Films, which Freedom Films believed might be liable in whole or in part for its claims under the letter agreement as alter egos of Nu Image and M3 Media.

2. The Petitions to Compel Arbitration and the Trial Court's Denial Orders

Nu Image and M3 Media petitioned to compel arbitration, and Freedom Films opposed the petition. Based on the parties' written submissions and after hearing argument, the trial court denied the petition to compel arbitration. The court stated, "The [letter] agreement, which is dated in January of 2009, which is attached to the complaint, does not expressly incorporate by reference either the distribution agreement or the settlement agreement. In fact, given the dates, the settlement agreement itself was not even in effect—or at least the writing was not finalized at the time the letter agreement which is the subject of this action was executed. That execution preceded the settlement agreement by a couple of weeks. Not only does the letter agreement not expressly incorporate the settlement agreement, nor could it be inferred that it was intended to incorporate provisions such as an arbitration agreement or dispute resolution provision in a settlement agreement that was not yet effected. As to the distribution agreement, the letter agreement provides that Freedom Films has the same audit rights as those enjoyed by Nu Image under the distribution agreement; and if you go to that portion of the distribution agreement, the audit rights provision is not where the arbitration agreement is provided, but it's in a different part of that agreement. Noteworthy to the court, the provisions of the distribution agreement in toto are not expressly incorporated into the letter agreement, nor was Freedom Films a party to the original distribution agreement. So . . . I'm making my ruling based on a preliminary finding that an enforceable arbitration agreement does not exist as between Freedom Films and Nu Image with respect to any disputes arising under the letter agreement. . . . I don't see how all three documents could be a part of the same overall agreement, but that's—at least with respect to the settlement agreement and the letter agreement, that argument is being made. I don't find that persuasive. The February 2009 settlement agreement is an agreement specifically between MGM on the one hand and Freedom Films and Nu Image on the other. The letter agreement appears to be a different standalone agreement as between Freedom Films and Nu Image. . . . It doesn't expressly or impliedly incorporate the arbitration provision from the settlement agreement."

Nu Image and M3 Media filed a notice of appeal. (Code Civ. Proc., § 1294, subd. (a) [order denying petition to compel arbitration appealable].) Meanwhile, the alleged alter ego defendants, Sacred Productions, Inc., Sacred Productions, LLC and Millennium Films, filed a petition to compel arbitration on the same grounds as those raised in the prior petition by Nu Image and M3 Media. The trial court denied that petition as well, concluding "that there

is no agreement to arbitrate as between these parties." Sacred Productions, LLC, Sacred Productions, Inc. and Millennium Films then filed a notice of appeal. (*Ibid.*) We consolidated the appeals.

DISCUSSION

"The right to arbitration depends upon contract; a petition to compel arbitration is simply a suit in equity seeking specific performance of that contract. [Citations.] (*Engineers & Architects Assn. v. Community Development Dept.* (1994) 30 Cal.App.4th 644, 653; see also *Brodke v. Alphatec Spine Inc.* (2008) 160 Cal.App.4th 1569, 1574.) As a result, a party seeking to compel arbitration "must allege the existence of an agreement to arbitrate the controversy[.]" (*Condee v. Longwood Management Corp.* (2001) 88 Cal.App.4th 215, 218, citing Code Civ. Proc., § 1281.2.) "Because the existence of the agreement is a statutory prerequisite [under Code of Civil Procedure section 1281.2] to granting [a] petition [to compel arbitration], the petitioner bears the burden of proving its existence by a preponderance of the evidence." (*Rosenthal v. Great Western Fin. Securities Corp.* (1996) 14 Cal.4th 394, 413.) "There is no public policy favoring arbitration of disputes [that] the parties have not agreed to arbitrate. [Citation.]" (*Engineers & Architects Assn.*, at p. 653; see also *Victoria v. Superior Court* (1985) 40 Cal.3d 734, 739 ["policy favoring arbitration cannot displace the necessity for a voluntary *agreement* to arbitrate"].) Standard rules of contract interpretation determine whether an agreement to arbitrate exists. (*Badie v. Bank of America* (1998) 67 Cal.App.4th 779, 787.) "We review the order denying the petition to compel arbitration de novo because the [trial] court did not resolve any factual disputes in rendering its decision. [Citation.]" (*Brodke*, at pp. 1573-1574.)

In this case, Freedom Films sues for breach of contract and fraud, and seeks an accounting, all based on allegations that Nu Image and M3 Media did not perform their obligations under the January 23, 2009 letter agreement to (1) pay Freedom Films its share of gross proceeds from *The Mechanic*, (2) comply with the letter agreement's accounting and audit provisions and (3) use good faith efforts to cast Presley in a lead role in the motion picture. The letter agreement did not contain an arbitration provision.

Absent an arbitration provision in the letter agreement, Nu Image and M3 Media, along with the alleged alter ego defendants, contend that this dispute is subject to the dispute resolution provision in the 2006 distribution agreement between Nu Image and MGM. They maintain that, because the letter agreement defined Freedom Films's accounting and audit rights in accordance with the accounting and audit provision and schedule in the distribution agreement, this dispute between Freedom Films and Nu Image, which encompasses Freedom Films accounting and audit rights under the letter agreement, should go to arbitration in accordance with the dispute resolution provision in the distribution agreement. We disagree. The letter agreement referred to the distribution agreement only to the extent that it defined Freedom Films's accounting and audit rights with respect to motion pictures like *The Mechanic*. The letter agreement did not incorporate the distribution agreement as a whole, nor did it make any reference to its dispute resolution provision or its exhibit outlining

the dispute resolution procedures. Under these circumstances, the dispute resolution provision in the distribution agreement does not require Freedom Films to arbitrate disputes or rights arising under the letter agreement. (See *Amtower v. Photon Dynamics, Inc.* (2008) 158 Cal.App.4th 1582, 1608 ["subject document must contain some clear and unequivocal reference to the fact that the terms of the external document are incorporated"]; cf. *Slaughter v. Bencomo Roofing Co.* (1994) 25 Cal.App.4th 744, 748-749 [subcontractor bound by arbitration provision in construction contract because subcontracts incorporated by reference "all of the terms and conditions of the Contract Documents" (emphasis added)]; *Boys Club of San Fernando Valley, Inc. v. Fidelity & Deposit Co.* (1992) 6 Cal.App.4th 1266, 1272 [surety in performance bond bound by arbitration agreement in construction contract or subcontract when external document as a whole is incorporated by reference into the bond].)

Nu Image and M3 Media, and the alleged alter ego defendants, also contend that this dispute is subject to arbitration because the Settlement Agreement entered into by MGM, on the one hand, and Nu Image, Home of the Brave Productions and Freedom Films, on the other hand, incorporated the dispute resolution provision in the distribution agreement. But the letter agreement on which this action is based made no reference to the Settlement Agreement, let alone referred to the dispute resolution provision from the distribution agreement incorporated into the Settlement Agreement. Indeed, the Settlement Agreement was executed *after* the letter agreement between Nu Image and Freedom Films, and disputes regarding the letter agreement, therefore, could not have been dependent on a reference to the distribution agreement in the Settlement Agreement. (*Gilbert Street Developers, LLC v. La Quinta Homes, LLC* (2009) 174 Cal.App.4th 1185, 1194 ["what is being incorporated must *actually exist at the time of the incorporation*, so the parties can know exactly what they are incorporating".]) In addition, although the Settlement Agreement was conditioned upon execution of the "Term Sheet," it was not so conditioned on the letter agreement, which was between Nu Image and Freedom Films. And, because the Settlement Agreement resolved claims in which Nu Image and Freedom Films were on the same side as against MGM, dispute resolution referenced in that agreement would not encompass disputes between Nu Image and Freedom Films with respect to matters, including accounting and audit rights, to which they had agreed separately, as between themselves, in the letter agreement. Although the Settlement Agreement encompassed *The Mechanic* by virtue of the "Term Sheet," the rights involved in the Settlement Agreement were different from those being litigated in this case between Freedom Films and Nu Image. The Settlement Agreement, therefore, does not bind Freedom Films to arbitrate this dispute.^[3]

As a result, neither of the theories advanced by Nu Image and M3 Media, and the alleged alter ego defendants, entitles them to arbitration.

DISPOSITION

The orders are affirmed. Freedom Films is entitled to recover its costs on appeal.

MALLANO, P. J. and CHANEY, J., concurs.

[1] The distribution agreement's dispute resolution provision and accompanying exhibit outlining the dispute resolution procedures provided that, in the event of "[a]ny controversy, claim, or dispute arising out of or related to this [distribution] [a]greement or the interpretation, performance, or breach hereof, including but not limited to alleged violations of state or federal statutory or common law rights or duties[.]" the parties shall meet and attempt in good faith to reach a negotiated resolution and, if unable to do so, call upon a retired judge or justice of any California state or federal court to mediate the dispute. If the parties are unable to resolve the dispute by mediation, then either party may initiate arbitration of the dispute.

[2] The Settlement Agreement provided, "[a]ny controversy, claim, or dispute arising out of or related to this Settlement Agreement or the interpretation, performance, or breach hereof, including but not limited to alleged violations of state or federal statutory or common law rights or duties (individually and collectively, 'Dispute') shall be resolved according to the procedures set forth in the Distribution Agreement."

[3] Nu Image and M3 Media, and the alleged alter ego defendants, additionally argue that it was for the arbitrator to decide whether this dispute was subject to arbitration. But they did not prove, as statutorily required, the existence of an arbitration agreement between them and Freedom Films over the rights under the letter agreement being sued on in this case. (See *Rosenthal v. Great Western Fin. Securities Corp.*, *supra*, 14 Cal.4th at p. 413.) Accordingly, the scope of an arbitration provision, which could be subject to the arbitrator's decision, is not an issue. In addition, Nu Image and M3 Media, and the alleged alter ego defendants, requested that we take judicial notice of the February 10, 2009 "Term Sheet" between Nu Image and MGM. Because they did not provide a basis for judicial notice under Evidence Code section 452, and in any event the "Term Sheet" does not affect our decision in this case, we deny the motion for judicial notice.