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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

ELEMENTS SPIRITS, INC., a California corporation;)	Case No. CV 15-02692 DDP (AGRx)
FABRICA DE TEQUILAS FINOS S.A. De C.V., a Mexican corporation; WORLDWIDE BEVERAGE IMPORTS, LLC, a Nevada limited liability company,)	
)	ORDER DENYING IN PART AND GRANTING IN PART MOTION TO DISMISS COUNTERCLAIMS
)	[Doc. No. 34]
)	
Plaintiffs,)	
)	
v.)	
)	
ICONIC BRANDS, INC., a California corporaiton;)	
GRACE KIM BRANDI, an individual,)	
)	
Defendants.)	
)	

Presently before the Court is Plaintiffs and Counterdefendants Elements Spirits, Inc., Fabrica de Tequilas Finos S.A. de C.V., and Worldwide Beverage Imports, LLC's Motion to Dismiss certain counterclaims from Defendants and Counterclaimants Iconic Brands, Inc. and Grace Kim Brandi's First Amended Counterclaim. Having heard oral arguments and considered the parties' submissions, the Court adopts the following order.

1 **I. BACKGROUND**

2 Plaintiff and Counterdefendant Elements Spirits, Inc.
3 ("Elements") sells KAH brand tequila. (First Am. Countercl. at 5.)
4 The tequila is bottled in painted, skull-shaped glass bottles meant
5 to resemble "'calaveras,' the decorated sugar skulls associated
6 with 'Dia de los Muertos.'" (Id. at 4-5.) Defendant and
7 counterclaimant Grace Kim Brandi ("Brandi") formed Elements in
8 November 2009, and Elements launched KAH Tequila in 2010. (Id. at
9 4-5.) In March 2010, Elements and Brandi were sued by Globefill,
10 Inc. for trade dress infringement over the skull-shaped bottles.
11 (Id. at 5.)

12 In June 2010, Elements sold 51% of its shares to Worldwide
13 Spirits, a company Defendants describe as "closely related to"
14 Plaintiff and Counterdefendant Worldwide Beverage Imports, LLC
15 ("Worldwide"). (Id. at 5.) In April 2011, Brandi was removed as
16 an officer and director of Elements, but she remained a minority
17 shareholder of the company. (Id. at 5-6.) In August 2011, Brandi
18 registered copyrights to the tequila bottle designs in her name.
19 (Id. at 6, exs. 1-5.)

20 In November 2013, during a mediation ordered in the Globefill
21 trademark litigation, Elements and Brandi entered into a "Binding
22 Agreement" in which "Brandi agreed to license her copyrighted
23 designs to Elements." (Id. at 7.) In exchange, Elements agreed to
24 pay for the defense of the Globefill suit, acknowledge Brandi as an
25 Elements shareholder, "conduct a proceeding to determine who [were]
26 the shareholders of Elements," "acknowledge Brandi as the creator
27 of KAH tequila brand and bottles," "acknowledge the validity of
28 Brandi's copyrights," and "provide annual statements of the

1 distribution status for the Elements shareholders." (Id. at 7-8.)

2 Sometime after entering into the agreement, relations
3 deteriorated between Brandi and Plaintiffs. (See id. at 8-11.)
4 Defendants allege that Plaintiffs failed to follow through with the
5 Binding Agreement. (Id. at 8-10.) So Brandi started a new
6 company, Defendant and Counterclaimant Iconic Brands, Inc.
7 ("Iconic"), and began selling another tequila using her copyrighted
8 designs. (Id. at 11.) Elements, Fabrica de Tequilas Finos S.A. de
9 C.V. ("Finos"), and Worldwide (collectively, "Plaintiffs" and
10 "Counterdefendants") then brought this case against Iconic and
11 Brandi (collectively, "Defendants" and "Counterclaimants") for
12 various claims, including trademark and trade dress infringement,
13 breach of contract, and business torts.

14 Iconic and Brandi responded with a counterclaim (now First
15 Amended Counterclaim or "FAC") against Plaintiffs, two of
16 Plaintiffs' corporate officers (Luz Maria Cabo Alvarez and Delia
17 Rodriguez Cabo), and two distributors of Plaintiffs' tequila,
18 Aveniu Brands, Inc. and Wine Warehouse. The counterclaims allege
19 (1) federal copyright infringement; (2) fraud in the inducement;
20 (3) breach of contract; (4) declaratory relief for rescission of
21 the Binding Agreement; (5) account stated; and (6) accounting.

22 Plaintiffs have now filed a Motion to Dismiss counterclaims
23 (2) fraud in the inducement, (5) account stated, and (6)
24 accounting.

25 **II. LEGAL STANDARD**

26 A 12(b)(6) motion to dismiss requires a court to determine the
27 sufficiency of the plaintiff's complaint and whether or not it
28 contains a "short and plain statement of the claim showing that the

1 pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2). Under
2 Rule 12(b)(6), a court must (1) construe the complaint in the light
3 most favorable to the plaintiff, and (2) accept all well-pleaded
4 factual allegations as true, as well as all reasonable inferences
5 to be drawn from them. See Sprewell v. Golden State Warriors, 266
6 F.3d 979, 988 (9th Cir. 2001), amended on denial of reh'g, 275 F.3d
7 1187 (9th Cir. 2001); Pareto v. F.D.I.C., 139 F.3d 696, 699 (9th
8 Cir. 1998).

9 In order to survive a 12(b)(6) motion to dismiss, the
10 complaint must "contain sufficient factual matter, accepted as
11 true, to 'state a claim to relief that is plausible on its face.'" Ashcroft v. Iqbal, 556 U.S. 662, 663 (2009) (quoting Bell Atl.
12 Corp. v. Twombly, 550 U.S. 544, 570 (2007)). However,
13 "[t]hreadbare recitals of the elements of a cause of action,
14 supported by mere conclusory statements, do not suffice." Id. at
15 678. Dismissal is proper if the complaint "lacks a cognizable
16 legal theory or sufficient facts to support a cognizable legal
17 theory." Mendiondo v. Centinela Hosp. Med. Ctr., 521 F.3d 1097,
18 1104 (9th Cir. 2008); see also Twombly, 550 U.S. at 561-63
19 (dismissal for failure to state a claim does not require the
20 appearance, beyond a doubt, that the plaintiff can prove "no set of
21 facts" in support of its claim that would entitle it to relief). A
22 complaint does not suffice "if it tenders 'naked assertion[s]'
23 devoid of 'further factual enhancement.'" Iqbal, 556 U.S. at 678
24 (quoting Twombly, 550 U.S. at 556). "A claim has facial
25 plausibility when the plaintiff pleads factual content that allows
26 the court to draw the reasonable inference that the defendant is
27 liable for the misconduct alleged." Id. The Court need not accept
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1 as true "legal conclusions merely because they are cast in the form
2 of factual allegations." Warren v. Fox Family Worldwide, Inc., 328
3 F.3d 1136, 1139 (9th Cir. 2003).

4 **III. DISCUSSION**

5 **A. Fraudulent Inducement Counterclaim**

6 Plaintiffs argue that the fraudulent inducement counterclaim
7 should be dismissed because the FAC fails to meet Rule 9(b)'s
8 particularity requirement by not pleading sufficient facts to
9 support the claim. (Mot. Dismiss at 5-6.) Defendants argue the
10 FAC alleges that Elements induced Brandi to agree to the "Binding
11 Agreement" but had no intention of performing the terms of the
12 agreement, thus sufficiently pleading fraud under Rule 9(b).
13 (Opp'n Mot. Dismiss at 6:1-3.) Plaintiffs respond that the
14 pleading is conclusory and fraudulent intent cannot be proven by
15 mere subsequent nonperformance of a contract. (Reply Supp. Mot.
16 Dismiss at 2-3.)

17 Federal Rule of Civil Procedure 9(b) requires a party to state
18 with "particularity the circumstances constituting fraud or
19 mistake." Fed. R. Civ. P. 9(b). "To satisfy Rule 9(b), a pleading
20 must identify the who, what, when, where, and how of the misconduct
21 charged, as well as what is false or misleading about [the
22 purportedly fraudulent] statement, and why it is false." Cafasso
23 v. Gen. Dynamics C4 Sys., Inc., 637 F.3d 1047, 1055 (9th Cir.
24 2011) (internal quotation marks and citations omitted). The
25 purpose of Rule 9(b)'s requirements is to provide the defending
26 party with notice of the particular averment of fraud so as to
27 allow the party to fully defend against the claim. See Bly-Magee
28 v. California, 236 F.3d 1014, 1019 (9th Cir. 2001).

1 Here, Brandi's theory for her fraud in the inducement claim is
2 that Elements, acting through its president and officer Timothy
3 Owens, convinced Brandi to enter into the Binding Agreement so
4 Elements could continue using Brandi's copyrighted designs in the
5 tequila bottles, but that Elements never intended to perform the
6 terms of the Agreement. (First Am. Countercl. at 8-10, 13-14;
7 Opp'n Mot. Dismiss at 5-6.) Section IV of the FAC details Brandi's
8 allegations that support a claim of fraud against Elements. (First
9 Am. Countercl. at ¶¶ 22-27.) Brandi claims that after she licensed
10 her copyrights to Elements in the Binding Agreement, Elements
11 "ceased acknowledging Brandi as the creator of KAH . . . ; . . .
12 failed to conduct the promised proceeding to determine the
13 shareholder status of the company; and . . . failed to provide any
14 annual statements of shareholders' distribution status for 2013 or
15 2014," all in violation of the Binding Agreement. (First Am.
16 Countercl. at ¶ 26.)

17 Additionally, the FAC points to Mr. Owens' declaration to this
18 Court in a prior preliminary injunction hearing, where Mr. Owens
19 stated that "Elements did not believe Brandi's copyrights were
20 valid" at the time Mr. Owens signed the Binding Agreement on
21 Elements' behalf. (First Am. Countercl. at 13.) Brandi argues
22 that this statement demonstrates that Elements entered into the
23 Binding Agreement without intending to perform its end of the
24 bargain.

25 Whether this argument ultimately succeeds is not the question
26 in a motion to dismiss based on Rule 9(b); instead, Brandi need
27 only put Elements on notice of the specific averment of fraud.
28 Here, the FAC contains sufficient pleading to put Elements on

1 notice of Brandi's specific averment of fraud against the company
2 in terms of who (Elements and Owens), what (not intending to follow
3 through on the Binding Agreement and abide by the terms), where (in
4 the Binding Agreement), when (at the Globefill mediation), why (to
5 get licenses to the copyrights), and how (promising to perform the
6 Binding Agreement), which is all the rule requires.

7 Elements also contends that Brandi's claim must fail because
8 she has not alleged any actions that constitute fraud. The "mere
9 failure to perform a contract does not constitute fraud," but "a
10 promise made without the intention to perform can be actionable
11 fraud." Richardson v. Reliance Nat'l Indem. Co., No. C 99-2952
12 CRB, 2000 WL 284211, at *4 (N.D. Cal. Mar. 9, 2000) (internal
13 quotations and citations omitted). Brandi's theory is not that
14 Elements merely failed to perform the contract. Rather, Brandi
15 pleads facts to show that Elements entered into the Binding
16 Agreement with no intention of actually performing its side of the
17 agreement. Altogether, the FAC's allegations demonstrate that
18 Brandi has pled sufficient facts to support her claim that Elements
19 entered into the Binding Agreement without the intention to perform
20 its obligations, which constitutes a proper allegation of fraud.

21 **B. Account Stated Counterclaim**

22 Iconic has an account stated counterclaim against Finos,
23 alleging that Finos did not pay a Chinese manufacturer of the KAH
24 tequila bottles for the manufacturer's work. (First Am. Countercl.
25 at 16; Opp'n Mot. Dismiss at 7:11-14.) Iconic alleges that the
26 manufacturer, Qingdao ABAC Glass Co., Ltd. ("ABAC Glass"), assigned
27 its claim against Finos for \$564,000 to Iconic. (First Am.
28 Countercl. at 16; Opp'n Mot. Dismiss at 7:21-22.) Finos argues the

1 Court lacks jurisdiction over this counterclaim because the
2 counterclaim does not arise out of the same transaction or
3 occurrence as the claims in the complaint. (Mot. Dismiss at 8-9.)
4 In response, Iconic argues that the "complaint's principal issues
5 all relate to the KAH tequila bottle," so the Court should exercise
6 jurisdiction over the counterclaim as it arises out of the same
7 transactions and occurrences as the complaint. (Opp'n Mot. Dismiss
8 at 8.) Further, doing so "best serves the interests of judicial
9 economy." (Id.)

10 **1. Compulsory Counterclaim**

11 A counterclaim may be either compulsory or permissive. Fed.
12 R. Civ. P. 13. If a counterclaim "arises out of the transaction or
13 occurrence that is the subject matter of the opposing party's
14 claim," the counterclaim is compulsory. Fed. R. Civ. P.
15 13(a)(1)(A). Because a compulsory counterclaim arises out of the
16 same transaction as the related claim, the two can be viewed as
17 part of the same case or controversy. Campos v. Western Dental
18 Servs., Inc., 404 F. Supp. 2d 1164, 1167 (N.D. Cal. 2005). Thus,
19 courts do have supplemental jurisdiction over compulsory
20 counterclaims.

21 To determine whether the claim and counterclaim arise out of
22 the same transaction, the court applies a "logical relationship"
23 test to "analyze whether the essential facts of the various claims
24 are so logically connected that considerations of judicial economy
25 and fairness dictate that all issues be resolved in one lawsuit."
26 Pochiro v. Prudential Ins. Co. of America, 827 F.2d 1246, 1249 (9th
27 Cir. 1987) (citation omitted).

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1 The account stated counterclaim requires the Court to inquire
2 into an agreement between Finos and ABAC Glass regarding the
3 manufacturing of the KAH tequila bottles and the alleged subsequent
4 failure to pay. The pertinent agreement to the claims in the
5 complaint is the Binding Agreement between Brandi and Elements,
6 which is an independent transaction and occurrence from the
7 agreement between Finos and ABAC Glass. Therefore, the
8 counterclaim is not compulsory and is instead permissive.

9 **2. Permissive Counterclaim**

10 Having determined that Iconic's account stated counterclaim is
11 permissive, the question remains whether this Court may exercise
12 supplemental jurisdiction over the counterclaim. The Ninth Circuit
13 has yet to express an opinion on whether permissive counterclaims
14 require an independent jurisdictional basis beyond 28 U.S.C. §
15 1367(a)'s "same case and controversy" requirement. Sparrow v.
16 Mazda American Credit, 385 F. Supp. 2d 1063, 1066-67 (E.D. Cal.
17 2005). The Second and Seventh Circuits, however, have held that 28
18 U.S.C. § 1367(a) allows district courts to exercise supplemental
19 jurisdiction over either compulsory or permissive counterclaims.
20 Jones v. Ford Motor Credit Co., 358 F.3d 205, 212-13 (2d Cir.
21 2004); Channell v. Citicorp Nat'l Servs., Inc., 89 F.3d 379, 384
22 (7th Cir. 1996).¹ The "same case and controversy" requirement for
23 supplemental jurisdiction under 28 U.S.C. § 1367(a) requires only a

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25 ¹ As other courts have noted, the extension of supplemental
26 jurisdiction to both compulsory and permissive counterclaims
27 renders the compulsory/permissive analysis somewhat redundant. See
28 Sparrow, 385 F. Supp. 2d at 1070 n.4. Those circuits which have
approved the exercise of supplemental jurisdiction have also
dispensed with the compulsory/permissive counterclaim inquiry. Id.
at 1067.

1 "loose factual connection between the claims." Channell, 89 F.3d
2 at 385.

3 Courts in this circuit have found they have discretion to
4 exercise supplemental jurisdiction over certain permissive
5 counterclaims. See, e.g., Marlin v. Chase Cardmember Servs., No.
6 1:09cv0192 AWI DLB, 2009 WL 1405196, *4 (E.D. Cal. May 19,
7 2009)(finding the court had discretion to exercise supplemental
8 jurisdiction over a breach of contract counterclaim on an
9 underlying debt in a Fair Debt Collection Practices Act case, but
10 declining to exercise such discretion).

11 Here, the complaint and counterclaim do share a loose factual
12 connection: the claims and counterclaims all revolve around the KAH
13 tequila bottles. Further, it is in the interest of judicial
14 economy to keep all the claims related to the parties and the KAH
15 tequila bottles together in one case. Therefore, the court in its
16 discretion will exercise supplemental jurisdiction over this claim.

17 **C. Accounting Counterclaim**

18 Brandi seeks an accounting against all Plaintiffs for profits
19 earned by the use and sale of Brandi's copyrights, the sales of KAH
20 tequila to determine the amount of royalties that should have been
21 paid to Elements, the attorney fees that are offsets against any
22 royalties earned by Elements, and the value of Brandi's stock in
23 Elements. (First Am. Countercl. at 17.) Plaintiffs argue that the
24 Copyright Act preempts Brandi's accounting claim. (Mot. Dismiss at
25 10:20-21.) Brandi responds that the accounting claim is not
26 preempted because the accounting claim is not based solely on her
27 claim for copyright infringement but is also based on her breach of
28 contract and fraud claims. (Opp'n Mot. Dismiss at 10.)

1 The Copyright Act preempts rights under common law or state
2 statutes that "are equivalent to any of the exclusive rights within
3 the general scope of copyright as specified by section 106." 17
4 U.S.C. § 301(a). The Ninth Circuit has adopted a two-part test for
5 copyright preemption. First, the court "determine[s] whether the
6 'subject matter' of the state law claim falls within the subject
7 matter of copyright as described in 17 U.S.C. §§ 102 and 103."
8 Laws v. Sony Music Ent'mt, Inc., 448 F.3d 1134, 1137 (9th Cir.
9 2006) (footnotes omitted). Second, if the court determines the
10 subject matter is within copyright, then the court "determine[s]
11 whether the rights asserted under state law are equivalent to the
12 rights contained in 17 U.S.C. § 106, which articulates the
13 exclusive rights of copyright holders." Id. at 1137-38.

14 **1. Subject Matter of Copyright**

15 First, the accounting claim must relate to subject matter
16 within the scope of the Copyright Act for preemption to apply.
17 Section 102 of the Copyright Act extends copyright protection to
18 "original works of authorship fixed in any tangible medium of
19 expression," including "sculptural works." 17 U.S.C. § 102(a).

20 Here, the first accounting claim in the FAC is for "all of
21 counterdefendants' profits earned as a result of their use and
22 sale, authorized and unauthorized, of counterclaimant Brandi's
23 copyrights." (First Am. Countercl. at 17). By its terms, this
24 claim relates to copyrightable subject matter—namely, Brandi's
25 copyrights in her sculptural works, the calavera-esque tequila
26 bottles.

27 The other three accounting claims are for the "sales of KAH
28 tequila, internationally, to determine what royalties should have

1 been paid to Elements"; the "attorney fees incurred and paid by
2 Elements or on its behalf that are being claimed as offsets against
3 royalties earned"; and "Elements' value and the value of
4 counterclaimant Brandi's stock in Elements." (First Am. Countercl.
5 at 17). These latter three claims are not grounded in the subject
6 matter of copyright because their subject matters are tequila
7 sales, attorneys fees, and values of a company and its stocks, none
8 of which are copyrightable. Thus, these three claims are not
9 within the scope of the Copyright Act, but the accounting for the
10 Plaintiffs' use of Brandi's copyrights is within the subject matter
11 of copyright.

12 **2. Exclusive Rights of Copyright**

13 Second, the right asserted in the state law action must be
14 equivalent to a right protected under the Copyright Act for
15 preemption to apply. Section 106 in the Copyright Act outlines the
16 exclusive rights of a copyright owner, including reproduction of
17 the copyrighted work, preparation of derivative works, distribution
18 of the work, and public performance and display of the work. 17
19 U.S.C. § 106(1)-(5). "To survive preemption, the state cause of
20 action must protect rights that are qualitatively different from
21 the rights protected by copyright: the complaint must allege an
22 'extra element' that changes the nature of the action." Grosso v.
23 Miramax Film Corp., 383 F.3d 965, 968 (9th Cir. 2004), amended on
24 denial of reh'g 400 F.3d 658 (9th Cir. 2004).

25 An accounting claim under California law requires a plaintiff
26 to show (1) a fiduciary relationship between the parties or (2)
27 complicated accounts such that "an ordinary legal action demanding
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1 a fixed sum is impracticable." Meixner v. Wells Fargo Bank, N.A.,
2 -F. Supp. 3d-, 2015 WL 1893514 (E.D. Cal. 2015).

3 An accounting between co-owners of a copyright is not
4 preempted by the Copyright Act because co-owners cannot sue each
5 other for infringement as they each have equal right to exploit the
6 work. See Oddo v. Ries, 743 F.2d 630, 633, 635 (9th Cir. 1984).
7 But where the cause of action for accounting is "rooted primarily
8 on contentions that [the other party] infringed on [the claimant's]
9 copyrighted work," then the Copyright Act does preempt the state
10 law claim. Motown Record Corp. v. George A. Hormel & Co., 657 F.
11 Supp. 1236, 1241 (C.D. Cal. 1987).

12 Here, Brandi's first accounting claim is based on Plaintiffs'
13 use of her copyrights. The validity of Brandi's copyrights as well
14 as the existence of a valid licensing relationship is disputed in
15 the complaint as well as the counterclaim. (See Compl. at 19-22;
16 First Am. Countercl. at 11-13, 15.) But what is most problematic
17 for this accounting claim is that Brandi makes a copyright
18 infringement claim against Plaintiffs, claiming that any license to
19 use her works was "cancelled" and that Plaintiffs "have made and
20 will make substantial profits and gains to which they are not
21 entitled" from such infringing use. (First Am. Countercl. at 12.)
22 Therefore, the accounting claim for profits derived from using
23 Brandi's copyrighted material is preempted by the Copyright Act
24 because it depends upon the resolution of the copyright
25 infringement claim.

26 **3. Lack of Legal Basis for Accounting**

27 Plaintiffs also argue that Brandi lacks a "legal basis" for
28 her accounting claims to determine the value of Elements and its

1 shares of stock. (Mot. Dismiss at 11.) In their Reply, Plaintiffs
2 further argue that the valuation claim and the other accounting
3 claims for attorneys fees and tequila sales are "derivative" and so
4 cannot be brought by Brandi as a direct suit. (Reply Supp. Mot.
5 Dismiss at 6-7.) To support her need for an accounting, Brandi
6 responds by pointing to the counterclaims for breach of contract
7 and fraud that are based in part on Plaintiffs' failure to provide
8 the requested information as promised in the Binding Agreement.
9 (Opp'n Mot. Dismiss at 10-11.)

10 Plaintiffs' argument is without merit because Brandi need not
11 bring these claims as a shareholder derivative suit. Brandi
12 alleges fraud in the inducement and breach of contract in relation
13 to Plaintiffs' actions after entering into the Binding Agreement.
14 It is upon these grounds that Brandi brings the accounting claims
15 for attorneys fees, tequila sales, and valuation of Elements and of
16 the shares in Elements. Brandi alleges that Plaintiffs' failure to
17 account as requested is a material breach of the Binding Agreement,
18 thus leading to Brandi's cancellation of any copyright licenses in
19 that Agreement. (See First Am. Countercl. at 10-11, 14, 17.)
20 Further, the lack of Plaintiffs' financial information prevents
21 Brandi from calculating any damages that could be owed for that
22 alleged breach and fraud. See Meixner, -F. Supp. 3d-, 2015 WL
23 1893514; Teselle v. McLoughlin, 173 Cal. App. 4th 156, 180
24 (2009)("[T]he purpose of the accounting is, in part, to discover
25 what, if any, sums are owed to the plaintiff.") Thus, Brandi
26 alleges a direct injury that is not required to be brought as a
27 derivative suit and that does have a legal basis at this motion to
28 dismiss stage.

1 **IV. CONCLUSION**

2 For the reasons stated above, Plaintiffs' Motion to Dismiss is
3 DENIED as to counterclaims (2) fraudulent inducement, (5) account
4 stated, and part of (6) accounting. The Motion is GRANTED with
5 prejudice as to the part of claim (6) accounting that is preempted
6 by the Copyright Act.

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8 IT IS SO ORDERED.

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11 Dated: September 17, 2015

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HON. DEAN D. PREGERSON
United States District Judge

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