UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

GOLDEN STATE EQUITY INVESTORS, INC.

Plaintiff,

v.

ALLIANCE CREATIVE GROUP, INC.

Defendant.

Case No.: 16cv1694-MMA (DHB)

ORDER DENYING DEFENDANT'S MOTION TO DISMISS FOR FAILURE TO STATE A CLAIM

[Doc. No. 6]

Plaintiff Golden State Equity Investors, Inc. filed the First Amended Complaint ("FAC") on September 1, 2016, against Defendant Alliance Creative Group, Inc. alleging a breach of contract. *See* Doc. No. 5, p. 7. Defendant now moves to dismiss the FAC for failure to state a claim upon which relief can be granted pursuant to Federal Rule of Civil Procedure 12(b)(6). *See* Doc. No. 6, p. 1. The Court took the matter under submission on the briefs and without oral argument pursuant to Civil Local Rule 7.1.d.1. *See* Doc. No. 11. For the reasons set forth below, the Court **DENIES** Defendant's motion to dismiss.

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I. BACKGROUND

Because this matter is before the court on a motion to dismiss, the Court must accept as true the allegations set forth in the FAC, but in doing so, does not make any findings of fact. *See Hosp. Bldg. Co. v. Trs. Of Rex Hosp.*, 425 U.S. 738, 740 (1976). Plaintiff alleges the following.

i. Overview

Plaintiff is an investment company focused on private money lending. *See* FAC ¶ 1. Defendant is a digital engagement company "engaged in the business of creative packaging." *See* FAC ¶ 2. Plaintiff and Defendant "have been in a contractual relationship for the past twelve (12) years." *See* Doc. No. 6-1, p. 2.

Specifically, on April 27, 2004, the parties entered into two agreements whereby Plaintiff invested $300,000.00 into Defendant's company in exchange for interest repayments and rights to purchase 3,000,000 shares of Common Stock. *See* FAC ¶ 7. The first agreement ("Original Note") stated that, starting on June 15, 2004, Defendant would pay 7 ¾ per annum interest rate on Plaintiff's $300,000.00 investment until the principal amount was paid in full. *See* FAC, Exh. C. The Original Note's maturity date was initially April 27, 2006. *See* FAC, Exh. C. The second agreement ("Warrant to Purchase Common Stock" or "Warrant") allowed Plaintiff the right to purchase 3,000,000 shares of Defendant's Common Stock. *See* FAC, Exh. B. The Warrant's expiration date was initially April 27, 2006. *See* FAC, Exh. B.

Seven years later, on April 25, 2011, the parties entered into an "Addendum" with new terms. *See* FAC, Exh. D. The Addendum "extended the maturity date of the Original Note and the expiration date of the Warrant to April 25, 2012." *See* FAC ¶ 10; *see also* Doc. No. 6-1, p. 2. The Addendum further acknowledged that $143,847.00 of the principal balance remained outstanding under the Original Note. *See* FAC, Exh. D.

On March 18, 2013, the parties then entered into an "Exchange Agreement" whereby the Original Note (and its 7 ¾ per annum rate) was exchanged for a "New Note" in which Defendant agreed to pay Plaintiff the remaining outstanding balance of

$143,312.00 at a lower 3 ¾ per annum interest rate. *See* FAC, Exh. E. The Exchange Agreement provided for Defendant to issue Common Stock to Plaintiff pursuant to the New Note's terms. *See id.* at §2.21 (stating "[Defendant] shall honor all conversions of the New Note and shall deliver Underlying Shares in accordance with the terms, conditions and time periods set forth therein"); *see also id*. at §2.04 (stating "[a]ny Underlying Shares, when issued in accordance with the terms of the New Note will be duly and validly issued . . .").

The New Note's terms, signed by the parties on March 31, 2013, extended the maturity date of the principal outstanding balance to March, 6, 2018. *See* FAC, Exh. A. Furthermore, Section 3.1 in the New Note states "at the option of the Holder [Plaintiff], this Debenture may be converted, either in whole or in part, up to the full Principal Amount . . . into [Defendant's] Common Shares . . . ." *See* FAC, Exh. A. The New Note also contains various provisions outlining the terms of conversions or transfers of Common Stock to the Plaintiff. *See* FAC, Exh. A, art. 3 (titled "Conversion of Debenture").

On March 21, 2014, after the Exchange Agreement and New Note were signed, Plaintiff elected to purchase 100,000 shares of Defendant's Common Stock by sending Defendant a document titled "Warrant Notice of Exercise." *See* FAC, Exh. F. This document's subject line stated "Warrant Notice," and the request included a PDF attachment titled "ACGX Warrant Exercise 032114." *See id.* Moreover, the document stated Plaintiff made the request "*pursuant to the terms of the Warrant* to Purchase Common Stock (Conversion Warrants) issued by [Defendant] to [Plaintiff]." *See id.* (emphasis added). According to this request, Plaintiff paid "$50,000 as cash and $50,000 as a debit against the existing warrant credit balance" for Defendant's Common Stock. *See id.* Defendant accepted the payments and "issued the shares requested by Plaintiff" based on "the existing warrant credit balance." *See id.*; *see also* Doc. No. 10, p. 4.

On April 20, 2016, Plaintiff sent Defendant another Conversion Notice exercising Plaintiff's "option to convert $2,500 Principal Amount of the [New Note] into shares of

[Defendant's] Common Stock." *See* FAC, Exh. G. Plaintiff contends it made this Conversion Notice pursuant to Section 3.1 of the New Note. *See* FAC ¶ 18. When Defendant failed to deliver the shares, Plaintiff sent a demand letter to Defendant pursuant to section 3.2(b) of the New Note seeking "cash at 120% of the principal amount . . . plus the outstanding Warrant Credit balance." *See* FAC ¶ 20. Defendant did not make these payments.

As a result, Plaintiff filed this action for breach of contract. Plaintiff alleges two theories of liability. First, Plaintiff contends that, despite that the Exchange Agreement did not expressly extend the Warrant's expiration date, the parties' subsequent conduct impliedly extended the Warrant's expiration date. Thus, Defendant breached that implied agreement when it failed to deliver the shares requested on April 20, 2016. Second, Plaintiff contends Defendant breached the New Note when it refused to deliver the shares or provide cash pursuant to Plaintiff's demand letter. *See* FAC ¶¶ 25-28. Defendant contends the Court should dismiss Plaintiff's action for four reasons: (1) Plaintiff fails to attach a valid Warrant agreement as an exhibit; (2) Plaintiff fails to allege a breach under the New Note; (3) the New Note is invalid; and (4) the Statute of Frauds precludes liability. *See* Doc. No. 6-1, pp. 2, 3, 6, 8.

II. LEGAL STANDARD

A Rule 12(b)(6) motion to dismiss tests the sufficiency of the complaint. *Navarro v. Block*, 250 F.3d 729, 732 (9th Cir. 2001). A pleading must contain "a short and plain statement of the claim showing that the pleader is entitled to relief. . . ." Fed. R. Civ. P. 8(a)(2). However, plaintiffs must also plead "enough facts to state a claim to relief that is plausible on its face." Fed. R. Civ. P. 12(b)(6); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007). That is, the pleadings must contain factual allegations "plausibly suggesting (not merely consistent with)" a right to relief. *Twombly*, 550 U.S. at 545. The plausibility standard thus demands more than a "formulaic recitation of the elements of a cause of action," or "naked assertions devoid of further factual enhancement." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009). Instead, the complaint "must contain allegations of

underlying facts sufficient to give fair notice and to enable the opposing party to defend itself effectively." *Starr v. Baca*, 652 F.3d 1202, 1216 (9th Cir. 2011).

In reviewing a motion to dismiss under Rule 12(b)(6), courts must assume the truth of all factual allegations and must construe them in the light most favorable to the nonmoving party. *Cahill v. Liberty Mut. Ins. Co.*, 80 F.3d 336, 337–38 (9th Cir. 1996). The court need not take legal conclusions as true merely because they are cast in the form of factual allegations. *Roberts v. Corrothers*, 812 F.2d 1173, 1177 (9th Cir. 1987). Similarly, "conclusory allegations of law and unwarranted inferences are not sufficient to defeat a motion to dismiss." *Pareto v. FDIC*, 139 F.3d 696, 699 (9th Cir. 1998). In determining the propriety of a Rule 12(b)(6) dismissal, courts generally may not look beyond the complaint for additional facts. *United States v. Ritchie*, 342 F.3d 903, 908 (9th Cir. 2003). "A court may, however, consider certain materials—documents attached to the complaint, documents incorporated by reference in the complaint, or matters of judicial notice—without converting the motion to dismiss into a motion for summary judgment." *Id.* Where dismissal is appropriate, a court should grant leave to amend unless the plaintiff could not possibly cure the defects in the pleading. *Knappenberger v. City of Phoenix*, 566 F.3d 936, 942 (9th Cir. 2009).

III. Discussion

A. Timeliness of Defendant's Motion to Dismiss

As an initial matter, Plaintiff contends that this Court should not consider Defendant's motion to dismiss because Defendant filed the motion one day after the applicable deadline expired. *See* Doc. No. 8, p. 2; *see also* Fed. R. Civ. P. 12(a)(1); 15(a)(3); 6(a). Generally, public policy favors disposition of cases on their merits. *See Hernandez v. City of El Monte*, 138 F.3d 393, 399 (9th Cir. 1998). Coincidentally, the docket reflects that Plaintiff's FAC was also untimely by one day. *See* Doc. No. 5; *see also* Fed. R. Civ. P. 15(a)(1)(B) (dictating a 21-day deadline). This situation requires the Court to take an equitable approach and allow the case to proceed on the merits. Therefore, the Court deems both Plaintiff's FAC and Defendant's motion to dismiss to be

timely, and considers Defendant's motion to dismiss on the merits. *See Pioneer Investment Services Co. v. Brunswick Associates Ltd. Partnership*, 507 U.S. 380, 395 (1993).

B. Breach of Contract Under California Law

Under California law, "[a] cause of action for breach of contract requires proof of the following elements: (1) existence of the contract; (2) plaintiff's performance or excuse for nonperformance; (3) defendant's breach; and (4) damages to plaintiff as a result of the breach." *See CDF Firefighters v. Maldonado*, 158 Cal. App. 4th 1226, 1239 (2008). Likewise, "[a] cause of action for breach of implied contract has the same elements as does a cause of action for breach of contract, except that the promise is not expressed in words but is implied from the promisor's conduct." *See Yari v. Producers Guild of Am., Inc.*, 161 Cal. App. 4th 172, 182, 73 Cal. Rptr. 3d 803, 811 (2008).

C. Plaintiff's Implied Contract Theory

Plaintiff first contends the terms of the Warrant are valid and enforceable because the parties' conduct following the Exchange Agreement created an implied-in-fact contract extending the Warrant's expiration date. *See* FAC ¶¶ 25-28. By accepting payments "as a debit against the existing warrant credit balance" and "pursuant to the terms of the Warrant to Purchase Common Stock," Plaintiff contends Defendant's conduct constituted an implied agreement to extend the Warrant. *See* FAC ¶ 12, n. 1. Therefore, it appears that one of Plaintiff's theories of liability is that Defendant breached the Warrant when it failed to deliver shares in response to Plaintiff's April 20, 2016 Conversion Notice. *See* FAC ¶ 20. Regarding Plaintiff's implied contract theory, Defendant argues the Warrant expired on April, 25, 2012, and was "never renewed." *See* Doc. No. 6-1, p. 2.

i. Plaintiff sufficiently alleges the terms of an implied agreement.

Defendant contends this Court should dismiss the FAC because Plaintiff "inexplicably failed to attach a copy . . . or recite *verbatim* the material provisions" of a valid Warrant agreement because the Warrant agreement that Plaintiff includes as part of

its FAC is expired. *See* Doc. No. 6-1, p. 5. The argument that a plaintiff must attach a copy of a contract or recite its terms verbatim in order to state a claim for breach of contract has been squarely rejected by California courts. *See Miles v. Deutsche Bank National Trust Co.*, 236 Cal. App. 4th 394, 402 (2015). For example, in *Miles*, the court, following the California Supreme Court's ruling in *Construction Protective Services, Inc. v. TIG Specialty Ins. Co.*, 29 Cal. 4th 189, 199 (2002), rejected that very argument and stated that a plaintiff may "plead the legal effect of the contract rather than its precise language." *Miles*, 236 Cal. App. 4th at 402. Attaching a copy or reciting verbatim the material provision of a valid agreement is not "the *exclusive* means of pleading a contract." *Id.* (emphasis added).

Rather, and applicable here in an implied contract dispute, courts must look to see if the plaintiff pleads the agreement according to its legal effect. Defendant asserts Plaintiff has not done so sufficiently because the FAC "fail[s] to fully describe the terms of said Warrant agreement," and thus, the Court "cannot fully understand what the alleged relationship of the parties was." *See* Doc. No. 6-1, p. 8. Defendant further alleges there are no "reasonable details" of a valid Warrant in Plaintiff's FAC. *See* Doc. No. 6-1, p. 7. Plaintiff, however, alleges that the only implied term of the Warrant is that the expiration date was extended by the parties' conduct. *See* FAC ¶ 12, n. 1; *see also* Doc. No. 8, p. 8. In other words, all other terms of the Warrant agreement that the parties entered into in 2006 remain the same. The purpose of the Warrant appears to be to give Plaintiff a right to purchase Defendant's common stock. *See* FAC, Exh. B. Therefore, the Court must examine whether Plaintiff's FAC contains reasonable details suggesting the parties' conduct intended to extend the Warrant's expiration date. *See Goodrich & Pennington Mort. Fund, Inc. v. Chase Home Finance, LLC*, No. 05-CV-636-JLS, 2008 WL 698464, at *7 (S.D. Cal. Mar. 14, 2008).

A contract may either be express or implied. "An implied contract is one, the existence and terms of which are manifested by conduct." Cal. Civ. Code §1621; *see also Foley v. Interactive Data Corp.*, 47 Cal. 3d 654, 677 (1988) ("Generally, courts seek

to enforce the actual understanding of the parties to a contract, and in so doing may inquire into the parties' conduct to determine if it demonstrates an implied contract."). "Such implied-in-fact contract terms ordinarily stand on equal footing with express terms." *Foley*, 47 Cal. 3d at 677; *see also Northstar Financial Advisors Inc. v. Schwab Investments*, 799 F.3d 1036, 1054 (9th Cir. 2015) (finding the parties' conduct and the defendant's "representations" that the defendant would perform created the terms of an implied contract). As to the basic elements of a contract cause of action, "there is no difference between an express and implied contract." *See Division of Labor Law Enforcement v. Transpacific Transportation Co.*, 69 Cal. App. 3d 268, 275 (1997). "While an implied in fact contract may be inferred from the conduct, situation or mutual relations of the parties, the very heart of this kind of agreement is an intent to promise." *Id.* Depending on the facts, the parties' conduct can demonstrate the required "meeting of minds or an agreement" just as much as words on paper. *See Caron v. Andrew*, 133 Cal. App. 2d 412, 417 (1955); see *also Desny v. Wilder*, 46 Cal. 2d 715, 736 (1956) ("If made in fact, contracts may be established by direct evidence or they may be inferred from circumstantial evidence."). The existence of an implied contract based on the circumstances "is clearly a question of fact." *See Del E. Webb Corp. v. Structural Material Co.*, 123 Cal. App. 3d 593, 611 (1981).

In *Goodrich & Pennington*, the defendant, involved in a loan dispute with the plaintiff, moved to dismiss the plaintiff's breach of contract action for failing to allege a valid implied contract. *See Goodrich & Pennington*, 2008 WL 698464 at *4. The court, in examining whether a promise could be implied, looked to the parties' course of conduct surrounding the loan. *See id.* at *7. The *Goodrich & Pennington* court noted the defendant affirmatively acted "pursuant to its obligations" under a previous agreement. *See id.* Additionally, the defendant in *Goodrich & Pennington* "received a benefit" by accepting plaintiff's payments during the parties' disputed business dealings. *See id.* From this conduct, the court noted that the plaintiff "reasonably believed" the defendant would continue performing based on the parties' agreement. *See id.* Therefore, based on

the parties' conduct, the court held that the plaintiff sufficiently pled an implied-in-fact contract. *See id.*

Here, although Plaintiff acknowledges that the parties failed to expressly extend the Warrant's expiration in the Exchange Agreement, Plaintiff sufficiently alleges that the parties' conduct demonstrates the parties' actual understanding to extend the Warrant. *See* FAC, ¶ 12, n. 1, ¶ 17. Specifically, on March 21, 2014, after the Exchange Agreement and New Note were signed, Defendant issued 100,000 shares of Common Stock to Plaintiff in response to Plaintiff's "Warrant Notice of Exercise." *See* FAC ¶ 17. Similar to *Goodrich & Pennington*, Defendant performed pursuant to its prior obligations "of the Warrant" and accepted Plaintiff's payments. *See* FAC ¶ 17, *see also* FAC, Exh. F. Therefore, based on conduct, the FAC sufficiently alleges Plaintiff "reasonably believed" Defendant would continue performing pursuant the parties' previous Warrant agreement. *See Goodrich & Pennington Mort. Fund, Inc.*, 2008 WL 698464, at *7.

The Court is unpersuaded that, as Defendant argues in its reply brief, this transaction was a "one-off" transaction independent of the allegedly expired and invalid Warrant. *See* Doc. No. 10, p. 4. As an initial matter, the Court does not accept factual assertions outside of the FAC as true for the purposes of ruling on Defendant's 12(b)(6) motion. Further, the March 21, 2014 Notice of Exercise, which Defendant performed, specifically stated that Plaintiff's request for Defendant to issue Common Stock was "pursuant to the terms of the Warrant." *See* FAC, Exh. F. Additional language such as "Warrant Notice," "Warrant Exercise," and that "[t]he undersigned makes the representations and covenants set forth in *Article 5 of the Warrant to Purchase Common Stock* (Conversion Warrants)" in the Notice of Exercise all demonstrate the parties' intent to extend the Warrant. *See* FAC, Exh. F. Thus, the Court finds Plaintiff sufficiently pleads an implied agreement to extend the Warrant, the terms of which are included in the Warrant agreement attached as part of the FAC and detail Plaintiff's contractual right to purchase shares. Therefore, regarding Plaintiff's first theory of breach, Plaintiff sufficiently pleads the legal effect, nature, and character of an implied contract, and that

Defendant breached that implied contract. *See, e.g.*, *Zenith Ins. Co. v. Cozen O'Conner*, 148 Cal. App. 4th 998, 1011 (2007).

iii. The Statute of Frauds does not bar Plaintiff's action.

Also, Defendant contends that the alleged implied contract is barred by the statute of frauds and is therefore invalid. *See* Doc. No. 6-1, p. 6.

California's statute of frauds "declares several types of agreements 'invalid' unless 'they, or some note or memorandum thereof, are in writing and subscribed by the party to be charged or by the party's agent.'" *Westside Estate Agency, Inc. v. Randall*, 211 Cal. Rptr. 3d 119, 124-25 (Ct. App. 2016) (quoting Cal. Civ. Code § 1624(a)); *see also Texaco, Inc. v. Ponsoldt*, 939 F.2d 794, 799 (9th Cir. 1991). For example, an oral agreement "that by its terms is not to be performed within a year from the making thereof is invalid." Cal. Civ. Code § 1624(a)(1). The statute of frauds' primary evidentiary purpose is "to require reliable evidence of the existence and terms of the contract and to prevent enforcement through fraud or perjury of contracts never in fact made." *In re Estate of Duke*, 61 Cal. 4th 871, 889 (2015). "It is a well established rule in California that if, by its terms, performance of a contract *is possible within one year*, the contract does not fall within the statute [of frauds] even though it is probable that it will extend beyond one year." *Hopper v. Lennen & Mitchell*, 145 F.2d 364, 366 (9th Cir. 1944) (emphasis added). "The statute of frauds may be satisfied where . . . the contract provides that a buyer will select and acquire certain [property rights] after the original written contract is executed." *Alameda Belt Line v. City of Alameda*, 133 Cal. App. 4th 15, 22 (2003).

Defendant's argument fails because Plaintiff's performance under the Warrant was possible within one year. *See* FAC, Exh. B, §1.1. As Plaintiff argues, "Plaintiff could have exercised the monthly maximum amount of 15% over the course of eight months and purchased all 3,000,000 shares it had a right to purchase well before one year." *See* Doc. No. 8, p. 6. Because "performance of a contract is possible within one year," the

statute of frauds does not invalidate the alleged implied contract.[1] *See Hopper*, 146 F.2d at 366.

D. Plaintiff's Theory of Breach Based on the New Note

Lastly, it appears Plaintiff contends as a separate or alternative theory of liability that Defendant breached the New Note when Defendant "failed to deliver the shares [requested in the April 20, 2016 Conversion Notice]" to Plaintiff. *See* FAC ¶ 20. Specifically, the FAC alleges Defendant breached both sections 3.1 and 3.2 of the New Note when Defendant did not convert stock pursuant to Plaintiff's Conversion Notice or issue payment requested in the demand letter. *See* FAC, Exh. H.

Defendant alleges the "New Note cannot be an enforceable agreement without a valid Warrant to rely upon." *See id*. at p. 8. However, as discussed above, the Court finds Plaintiff's FAC sufficiently alleges the Warrant's expiration was impliedly extended through conduct. Thus, even assuming that the validity of the New Note is dependent on the validity of the Warrant agreement, Defendant's argument fails.

Also, Defendant argues that it owed no duty to convert the shares requested in the Conversion Notice. *See* Doc. No. 6-1, p. 9. Specifically, Defendant contends "the New Note clearly states that Plaintiff cannot issue a conversion notice to Defendant if the amount of shares contained in the conversion notice would put Plaintiff's ownership interest in Defendant's outstanding stock over 9.99%." *See* Doc. No. 6-1, p. 9. Defendant does not argue that conversion of the requested shares would have resulted in Plaintiff obtaining an ownership interest exceeding 9.99%, but rather, Defendant argues that Plaintiff must plead that conversion of the requested shares would *not* have had such a result. The Court is unconvinced that dismissal is warranted on that basis. Defendant's argument is less an argument that it did not have a duty to perform under the contract as much as it is an argument that Plaintiff must plead facts precluding the existence of any

[1] For that reason, the Court need not address the issues of partial performance and estoppel that Plaintiff raises.

potential defenses that Defendant might raise. However, "plaintiffs need not anticipate and attempt to plead around all potential defenses." *See Xechem, Inc. v. Bristol-Myers Squibb Co.*, 372 F.3d 899, 901 (7th Cir. 2004). Unless a plaintiff "pleads itself out of court" in the complaint, "[c]omplaints need not contain *any* information about defenses and may not be dismissed for that omission." *Id.*

Accordingly, the Court is unpersuaded that Defendant's arguments justify dismissal of the FAC.

IV. Conclusion

The Court, having considered all of Defendant's arguments, and for the reasons stated above, **DENIES** Defendant's motion to dismiss. *See* Doc. No. 6.

IT IS SO ORDERED.

Dated: April 7, 2017

Hon. Michael M. Anello
United States District Judge