

Koch Entertainment LP v Troma Entertainment, Inc.
2008 NY Slip Op 31120(U)
April 8, 2008
Supreme Court, New York County
Docket Number: 0600429/2007
Judge: Herman Cahn
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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT

Cahn

PART 49

Justice

Index Number : 600429/2007

KOCH ENTERTAINMENT LP

VS.

TROMA ENTERTAINMENT, INC.,

SEQUENCE NUMBER : # 001

DISMISS

INDEX NO. 600429-01

MOTION DATE #001

MOTION SEQ. NO.

MOTION CAL. NO.

ere read on this motion to/for

PAPERS NUMBERED

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits

Replying Affidavits

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

**MOTION IS DECIDED IN ACCORDANCE
WITH ACCOMPANYING MEMORANDUM
DECISION IN MOTION SEQUENCE**

FILED

APR 10 2008

COUNTY CLERK'S OFFICE
NEW YORK

Dated: April 8 2008

Jan C...

J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate

DO NOT POST

REFERENCE

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : IAS PART 49

-----X
KOCH ENTERTAINMENT LP,

Plaintiff,

-against-

Index No. 600429/07

TROMA ENTERTAINMENT, INC.,

Defendant.

-----X
TROMA ENTERTAINMENT, INC.,

Third-Party Plaintiff,

-against-

KOCH ENTERTAINMENT DISTRIBUTION LLC,
KOCH ENTERTAINMENT GP LLC, ENTERTAINMENT
ONE, LP, EARL STREET CAPITAL, LTD., MARWYN
CAPITAL, LLP, AND MARWYN INVESTMENT
MANAGEMENT, LLP,

Third-Party Defendants.

-----X
Herman Cahn, J.:

Third-party defendants Earl Street Capital, Ltd., Marwyn Capital, LLP and Marwyn Investment Management LLP (collectively, movants) move to dismiss the third-party complaint based on documentary evidence, failure to state a viable cause of action and lack of personal jurisdiction, CPLR 3211 (a) (1), (a) (7), and (a) (8).

The claims in the main action, the counterclaims and the third-party action claims arise out of a distribution agreement dated June 2, 2005. Pursuant to the agreement, defendant/third-party plaintiff Troma Entertainment, Inc., a New York film producer and video company, granted

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plaintiff Koch Entertainment LP's predecessor-in-interest, third-party defendant Koch Entertainment Distribution LLC, a Delaware media distribution company headquartered in New York, an exclusive license to market, distribute and sell Troma products in the United States and Canada. Prior to amendment, the agreement provided that its term would expire on July 31, 2006 in the United States and on August 31, 2006 in Canada. The agreement requires Troma to provide Koch with DVDs to distribute and to pay any negative monthly balances and other sums due. The agreement also requires Koch to pay Troma certain guaranteed minimum advance licensing fees in accordance with a fee schedule.

Troma alleges that in March 2006, it advised Koch that it would not renew the distribution agreement at the conclusion of its stated term. After negotiation, these companies amended the agreement to extend its term through December 31, 2007 in the United States and Canada and to require Koch to pay additional advance licensing fees.

On February 20, 2007, Koch sent Troma a notice of default and termination letter pursuant to section 13 (b) of the agreement based on allegations that Troma failed to keep certain DVD titles in stock. Koch alleges that Troma failed to cure the default within 30 days and that, therefore, the distribution agreement automatically terminated on March 30, 2007.

In the amended complaint, Koch asserts claims for breach of contract and account stated. It seeks to recover compensatory damages as will be proven at trial, together with costs of collection, including reasonable attorneys' fees. Specifically, Koch alleges that Troma failed to timely provide it with products and fill open orders, causing Koch to lose sales and damaging its relationships with certain retailers. Koch also alleges that Troma failed to pay the negative monthly balances due as well as other amounts, totaling \$164,000. Finally, Koch alleges that

Troma breached the distribution agreement's exclusivity provision and the covenant of good faith and fair dealing by directly selling Poultrygeist: Night of the Chicken Dead in DVD format to wholesalers and retailers.

Troma's answer denies all allegations of wrongdoing.

Troma has asserted counterclaims against Koch based on allegations of breach of contract. In the counterclaims, Troma alleges that on August 1, 2006, Koch advised Troma that it would not make the \$250,000 payment, due on August 5, 2006, in breach of the amended distribution agreement. The breach made it difficult for Troma to operate its own business and made it impossible for it to supply Koch with additional films for distribution. Troma alleges that in August and September 2006, Koch made payments against the outstanding balance, leaving \$160,000 still due and owing. Troma also alleges that Koch sold Troma DVDs at discount prices, thus decreasing Troma's profits, and that Koch has failed to account for the discounts or the manner in which they were calculated.

Troma has commenced a third-party action against movants, Koch Entertainment Distribution, and third-party defendants Koch Entertainment GP LLC, and Entertainment One, LP, for breach of contract based on factual allegations substantially similar to those it asserts in the counterclaims.

Troma has impleaded movants and Entertainment One, who are not signatories to the distribution agreement, on allegations that they are successors-in-interest to Koch. Specifically, Troma alleges that, during the agreement term, Entertainment One, a Canadian corporation, acquired the assets and liabilities of all three Koch entities. Troma further alleges that, as a result of the acquisition, Entertainment One assumed responsibility for the implementation and

execution of the distribution agreement. Troma also alleges that in February 2007, during the agreement term, Entertainment One sold the assets and liabilities of the Koch entities to movants Earl Street, a Cayman Islands corporation, and Marwyn Investment and Marwyn Capital, both organized under the laws of the United Kingdom. Earl Street then assumed the name of Entertainment One. Troma further alleges that, as a result of the acquisition transaction, Earl Street and both Marwyn entities assumed responsibility for the implementation and execution of the agreement.

In the first third-party claim, Troma alleges that third-party defendants breached the distribution agreement by failing to make advance payments in the amount of \$160,000, failing to provide an accounting, failing to use best efforts to market and sell Troma products, misrepresenting their efforts on Troma's behalf, holding more than 180,000 Troma DVDs without making any effort to sell them, engaging in self- and double-dealing by marketing and selling their own films to the exclusion and detriment of Troma and providing discounts to customers without explanation or an accounting to Troma. In the second cause of action, Troma alleges a breach of the agreement by failing to permit Troma to audit Koch's financial records. The third cause of action is for unjust enrichment by failing to pay \$160,000 in advance payments due under the agreement. In the fourth cause of action, Troma seeks a judgment declaring that third-party defendants breached the distribution agreement by failing to make advance payments, failing to provide an accounting, failing to use reasonable efforts, engaging in self- and double-dealing, providing discounts to its customers without explanation and ceasing to function as a Troma distributor, and that, therefore, Troma is entitled to terminate the agreement early.

Movants now seek to dismiss the third-party action as asserted against them, contending that this court lacks in personam jurisdiction over them on grounds that Troma has not alleged that they do business in New York and that they are foreign limited liability partnerships which do not do business in the United States.

In opposition, Troma contends that movants are doing business in New York and the United States through their subsidiaries, the three Koch entities, which are each headquartered in New York. Troma further contends that the motion is premature and that, at this early stage of the litigation, before movants have served an answer, Troma is entitled to conduct discovery to determine the nature and quality of movants' contacts with New York, directly and through Koch.

Sections 301 and 302 of the CPLR permit service of process on a foreign corporation outside New York, only where the corporation engages in a continuous and systematic course of doing business in New York (Landoil Resources Corp. v Alexander & Alexander Servs., Inc., 77 NY2d 28, 33-34 [1990]). "The test for 'doing business' is a 'simple [and] pragmatic one,' which varies in its application depending on the facts of a particular case . . . The court must be able to say from the facts that the corporation is 'present' in the State 'not occasionally or casually, but with a fair measure of permanence and continuity'" (*id.* [internal citations omitted]).

The systematic acts of a New York subsidiary or agent may be attributed to the foreign parent by two methods, either piercing the corporate veil or finding an agency relationship; the "mere ownership' of a subsidiary within the court's jurisdiction does not subject the non-domiciliary parent to jurisdiction under CPLR 301 or 302" (Timothy Lane Corp. v Gramercy Ins. Co., 1987 WL 15278 at *2-3 [EDNY 1987] [internal citations omitted]; Re v Breezy Point Lumber Co., 118 Misc 2d 206, 208 [Sup Ct, Queens Co. 1983]). "A subsidiary's acts confer

jurisdiction over the parent either where the subsidiary 'performs all the business' which the parent could do were it here by its own officials or where the parent's control over the subsidiary's activities [is] so complete that the subsidiary is, in fact, merely a 'department of the parent'" (Re v Breezy Point Lumber Co., 118 Misc 2d at 209 [internal citations omitted]). The mere formal separation between the parent and the subsidiary is not enough to shield the parent from the exercise of jurisdiction; the reality of the relationship is the final test (id.).

Here, there is no dispute that movants are foreign corporations, incorporated in either the United Kingdom or the Cayman Islands, and maintain no direct offices or employees in the United States. There is also no dispute that the Koch entities are headquartered in New York and do business in New York and that Koch is a signatory to the distribution agreement. Further, some transactions occurred during the term of the distribution agreement that affected the Koch entities' ownership.

However, the parties dispute whether the transfer of an equity interest in the Koch entities to Entertainment One and the subsequent transfer of an equity interest in Entertainment One to one or more of movants caused the Koch entities to become movants' subsidiaries and whether the relationship, if any, created contacts with New York sufficient to warrant an exercise of personal jurisdiction over movants.

Contracts and publicly available records, consisting primarily of news items based on press releases issued by Entertainment One, produced by movants indicate that Earl Street was created by Marwyn Investment for the purpose of acquiring Entertainment One. On February 14, 2007, Earl Street purchased a 100% equity interest in (the old) Entertainment One and its subsidiaries, including the Koch entities, for \$167 million (see also Throop Aff, ¶¶ 2, 7, 8, 10).

The organizational chart of Earl Street and Entertainment One indicates that Koch remained an indirectly wholly owned subsidiary of Entertainment One/Earl Street after the transaction (*id.*, ¶ 11).

From this evidence, it appears that Earl Street purchased Entertainment One, renamed itself Entertainment One, and advertised and promoted the Koch entities as its subsidiaries, a part of its family of companies. The evidence also suggests that the Marwyn entities used Entertainment One/Earl Street to acquire the Koch entities and financed the Koch operations in New York in order to expand Marwyn's presence in the United States. It also appears that movants purchased and began financing Koch prior to expiration of the distribution agreement.

Contrary to movants' contention, the record indicates that movants, including Earl Street, existed during the term of the distribution agreement. The court notes that the parties dispute whether the agreement naturally expired on December 31, 2007 or was earlier terminated by Koch on March 30, 2007. However, it appears that all three movants, including Earl Street, were created and purchased Entertainment One prior to either of these dates.

Movants' contention that they acquired "merely" an equity interest in the Koch entities' parent corporation and did not acquire the Koch entities' assets, liabilities or their obligations under the distribution agreement, raises factual issues which are incapable of resolution on the record now before the Court.

At this early stage of the litigation, and given the complex nature of the multiple transactions resulting in movants' acquisition of an interest in Entertainment One and the Koch entities, Troma is entitled to discovery of the acquisition documents, facts and circumstances surrounding the acquisitions, name changes, mergers and corporate transactions. For these

reasons, a framed issue hearing is required to determine the nature, quality and extent of movants' ownership interest in Entertainment One and the Koch entities and movants' control exerted over the Koch entities in order to determine whether a basis exists for the exercise of personal jurisdiction over movants. However, pending a final decision on these issues, discovery shall continue as to the issues of the Court's jurisdiction, and all the collateral issues relating thereto, and as to the issues raised in the complaint, answer and counterclaims. The parties, except for movants, shall comply with the terms of the preliminary conference order dated February 14, 2008.

Accordingly, it is

ORDERED that the issue of the Court's personal jurisdiction over third-party defendants Earl Street Capital, Ltd., Marwyn Capital, LLP and Marwyn Investment Management LLP is referred to a Special Referee to hear and report with recommendations; except that, in the event of and upon the filing of a stipulation of the parties, as permitted by CPLR 4317, the Special Referee, or another person designated by the parties to serve as referee, shall determine the aforesaid issue; and it is further

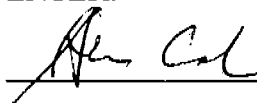
ORDERED that this motion is held in abeyance pending receipt of the report and recommendations of the Special Referee and a motion pursuant to CPLR 4403 or receipt of the determination of the Special Referee or designated referee; and it is further

ORDERED that counsel for the party seeking the reference or, absent such party, counsel for the third-party plaintiff shall, within 30 days from the date of this order, serve a copy of this order with notice of entry, together with a completed Information Sheet (available in room 119),

upon the Special Referee Clerk in the Motion Support Office (room 119), who is directed to place this matter on the calendar of the Special Referee's Part (Part 50R) for the earliest convenient date.

Dated: April 8, 2008

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