Filed 4/23/14 Alpert v. HAD Mortgage Fund CA2/3

NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION THREE

GLEN ALPERT, as trustee, etc., et al., Plaintiffs and Respondents, v. HDA MORTGAGE FUND, LLC, et al., Defendants and Appellants.	B247142 (Los Angeles County Super. Ct. No. BC487495)

APPEAL from an order of the Superior Court of Los Angeles County, Rita J. Miller, Judge. Reversed with directions.

Katten Muchin Rosenman, Alan D. Croll, Joel R. Weiner, Jennifer A. Lam and Danielle L. Raymond for Defendants and Appellants.

Dickstein Shapiro, James H. Turken and Michael I. Rothwell for Plaintiffs and Respondents.

HDA Mortgage Fund, LLC (Fund Co.), and HDA Properties Inc. (Properties) appeal the denial of their motion to compel arbitration of a complaint by Glen Alpert, as trustee of several trusts, and others (collectively, Plaintiffs). Properties, acting as the fund manager for Fund Co., is a party to arbitration agreements with Plaintiffs. Other defendants are not parties to the arbitration agreements. The trial court denied the motion to compel arbitration under Code of Civil Procedure section 1281.2, subdivision (c),[1] which establishes the third party litigation exception to the general rule requiring the enforcement of an agreement to arbitrate.

Fund Co. and Properties contend (1) the third party litigation exception is inapplicable, and (2) even if the exception applies, the trial court's refusal to order arbitration and stay either this action or the arbitration was an abuse of discretion. We conclude that the exception is inapplicable because the nonparties to the arbitration agreement are entitled to enforce the agreement and therefore are not "third parties" within the meaning of section 1281.2, subdivision (c). We therefore will reverse the order with directions.

FACTUAL AND PROCEDURAL BACKGROUND

1. *Factual Background*

Fund Co. invests in loans secured by deeds of trust and offers shares in an investment fund known as the HDA Mortgage Fund. Properties is the fund manager.

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[1] All statutory references are to the Code of Civil Procedure unless stated otherwise.

Harold Davidson & Associates, Inc. (HDA), provides investment counseling and portfolio management services. Harold A. Davidson is president of both HDA and Properties. David Mills is vice president of HDA and secretary of Properties.

Plaintiffs are investors, and Glen Alpert is their business manager.[2] Plaintiffs entered into Investment Counseling and Portfolio Management Agreements (Investment Counseling Agreements) with HDA granting HDA the authority to make and implement investment decisions on Plaintiffs' behalf in accordance with their investment objectives without prior consultation.[3] Acting under that authority, HDA invested Plaintiffs' money directly in loans secured by deeds of trust. HDA later advised Plaintiffs to invest in the HDA Mortgage Fund instead of investing directly in loans secured by deeds of trust. Plaintiffs purchased shares of the HDA Mortgage Fund beginning in late 2007 or

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[2] Plaintiffs are Glen Alpert, as trustee of the Manuel J. Cruz Living Trust dated May 20, 2004 (Cruz Trust), Hawkes Bay Pension Trust, William Sugarman Trust, and Alpert & Associates, Inc. Defined Benefits Pension Plan (Alpert & Associates Trust); Penny J. Alpert, individually and as trustee of the Renee Benell Trust; Marci Rosenberg, as trustee of the Renee Benell Trust; Regan and Ayesha Upshaw, as trustees of the Upshaw Family Trust; Eve L. Wolf; Joseph Hoffman; Craig Williams, as trustee of the Craig Williams Profit Sharing Plan (Williams Trust); James Dixon; Rebecca Marie; Paul Canter, individually and as trustee of the Paul Canter Retirement Trust; June Canter; Hammerhead Productions, Inc.; Dan Chuba, as trustee of the Hammerhead Productions Pension Plan; and Nicole Katz, as trustee of the Keepers Pension Trust.

[3] Plaintiffs allege that the sole exception is Williams, as trustee of the Williams Trust, who did not enter into an Investment Counseling Agreement with HDA.

early 2008.[4] HDA also caused Plaintiffs to exchange some of their investments in loans secured by deeds of trust for shares in the fund.

The HDA Mortgage Fund was governed by an Operating Agreement dated August 9, 2007, between Properties and the investors, known as members. Plaintiffs became members by signing a Subscription Agreement, which was accepted by Properties. The Operating Agreement included an arbitration provision stating:

"Any action to resolve any controversy or claim arising out of or related to this Agreement, or the breach hereof, however characterized, shall be resolved through a binding, non-public arbitration before an adjudicator selected as provided in this Article 11."

The Operating Agreement stated that "[t]he hearing . . . shall be conducted pursuant to the provisions of the California Arbitration Act commencing with California Code of Civil Procedure Section 1280, the rules and procedures established by JAMS, and such other rules and procedures as may be determined by the adjudicator . . . . " It also stated that the arbitrator must determine all issues, including arbitrability:

"The adjudicator shall try all of the issues, including any issues that may be raised concerning arbitrability of the dispute, subject-matter and personal jurisdiction, and any and all other issues, whether of fact or law, and shall hear and decide all motions and matters of any kind."

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[4] Plaintiffs allege that Penny Alpert and Glen Alpert, as trustee of the Alpert & Associates Trust, are the only plaintiffs who did not purchase shares of the HDA Mortgage Fund.

2. *Complaint*

Plaintiffs filed a complaint in July 2012 against HDA, Fund Co., Properties, Davidson, and Mills. Plaintiffs allege that HDA, with the assistance of each of the other defendants, provided them with quarterly investment reports known as "Portfolio Appraisals." Plaintiffs allege that the Portfolio Appraisals throughout 2008 were false and misleading in that they failed to accurately reflect the declining value of Plaintiffs' investments both in the HDA Mortgage Fund and outside the fund. They allege that many of the deeds of trust were in default, yet HDA, with the assistance of each of the other defendants, reported the loans as fully performing and continued to encourage Plaintiffs to invest in the HDA Mortgage Fund. Plaintiffs also allege that Fund Co. breached its obligations under the Operating Agreement by investing in loans that did not satisfy the fund's guidelines and that the defendants imposed management fees based on artificially inflated investment values.

Plaintiffs allege that Glen Alpert became suspicious and, on October 15, 2008, demanded that Defendants return Plaintiffs' investments. Defendants failed to do so and announced the closing of the HDA Mortgage Fund in a letter dated November 30, 2008.

Plaintiffs also allege that HDA, Davidson, and Mills provided misleading information and a sham appraisal relating to an investment known as Desert Hot Springs Property, in which two of the plaintiffs invested. They allege that after the Desert Hot Springs loan was in default, the defendants arranged to swap the investments of other investors in Desert Hot Springs for shares in the HDA Mortgage Fund, to the

detriment of the fund. Plaintiffs allege that HDA, with the assistance of Davidson and Mills, later notified them in April 2009 that the property was unsuitable for development.

Plaintiffs allege counts for (1) fraudulent misrepresentation, by all plaintiffs against all defendants; (2) fraudulent concealment, by all plaintiffs against all defendants; (3) negligent misrepresentation, by all plaintiffs against all defendants; (4) breach of fiduciary duty, by all plaintiffs against HDA, Properties, and Davidson; (5) constructive fraud, by all plaintiffs against all defendants other than Mills; (6) breach of contract (Investment Counseling Agreements), by all plaintiffs except Williams, as trustee of the Williams Trust, against HDA; (7) breach of the implied covenant of good faith and fair dealing (Investment Counseling Agreement), by all plaintiffs except Williams, as trustee of the Williams Trust, against HDA; (8) breach of contract (Operating Agreement), by all plaintiffs except Penny Alpert and Glen Alpert, as trustee of the Alpert & Associates Trust, against Fund Co.; and (9) breach of the implied covenant of good faith and fair dealing (Operating Agreement), by all plaintiffs except Penny Alpert and Glen Alpert, as trustee of the Alpert & Associates Trust, against Fund Co.

3. *Motion to Compel Arbitration*

Fund Co. and Properties moved to compel arbitration of all counts alleged against them in the complaint and either dismiss or stay those counts pending the completion of the arbitration. They argued that Plaintiffs were all parties to the Operating Agreement and that all of the counts alleged against the moving defendants

were within the scope of the arbitration provision in the Operating Agreement. They argued that any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration or decided by an arbitrator.[5] They did not address section 1281.2, subdivision (c) in their motion.

Counsel for Fund Co. and Properties also represented the other defendants, who jointly demurred to the complaint. Counsel stated in the motion to compel arbitration that they "reserve the right to compel arbitration with respect to the other defendants . . . when the pleadings become more clearly defined."

Plaintiffs argued in opposition that they never agreed to arbitrate disputes arising from the Investment Counseling Agreements and that they were not parties to any arbitration agreement with HDA, Davidson, or Mills. They argued that their claims against those nonmoving defendants relating to investment counseling services were inextricably intertwined with their claims against Fund Co. and Properties relating to their investments in the HDA Mortgage Fund, and that all of the defendants participated in the same fraudulent scheme. Plaintiffs argued that there was a possibility of conflicting rulings if their potentially arbitrable claims against Fund Co. and Properties relating to their investments in the HDA Mortgage Fund were arbitrated and their

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[5] Fund Co. and Properties filed a declaration by their counsel stating that Rule 11(c) of the JAMS Comprehensive Arbitration Rules and Procedures provided: "Jurisdictional and arbitrability disputes, including disputes over the formation, existence, validity, interpretation or scope of the agreement under which arbitration is sought, and who are proper Parties to the Arbitration, shall be submitted to and ruled on by the Arbitrator. The Arbitrator has the authority to determine jurisdiction and arbitrability issues as a preliminary matter."

nonarbitrable claims against the other defendants relating to investment counseling services were litigated in court. They argued that the trial court therefore should decline to compel arbitration pursuant to section 1281.2, subdivision (c).

Fund Co. and Properties argued in reply that the claims against them relating to the operation of the HDA Mortgage Fund pursuant to the Operating Agreement were separate and distinct from the claims against HDA, Davidson, and Mills relating to investment counseling services provided pursuant to the Investment Counseling Agreements. They argued that the claims involved "different agreements, different obligations, different standards, different relationships, and different transactions." They argued that section 1281.2, subdivision (c) was inapplicable because Plaintiffs had failed to show that the arbitrable and nonarbitrable claims "aris[e] out of the same transaction or series of related transactions" (*ibid.*) and that "there is a possibility of conflicting rulings on a common issue of law or fact" (*ibid.*).

Fund Co. and Properties also argued in reply that if, as Plaintiffs argued, the claims against Fund Co. and Properties were closely interrelated with the claims against the other defendants, section 1281.2, subdivision (c) was inapplicable because there was no "third party" (*ibid.*) in this litigation who was not subject to the arbitration agreement. They argued that this was so because Plaintiffs were equitably estopped from refusing to arbitrate with HDA, Davidson, and Mills as nonsignatories to the arbitration agreement if, as Plaintiffs argued, their claims against those defendants were inextricably intertwined with the contractual obligations in the contract containing the arbitration clause (i.e., the Operating Agreement). They also argued that Davidson and

Mills as agents of Properties had a right to enforce the arbitration agreement and therefore were not third parties for purposes of the statute.

Fund Co. and Properties argued further that even if section 1281.2, subdivision (c) applied, the trial court should exercise its discretion under the statute to order the parties to the arbitration agreement to arbitrate while staying the action as to other parties pending the completion of the arbitration, or stay the arbitration pending the completion of the litigation. They argued that in light of those alternatives, the court should not deny arbitration outright.

The trial court issued a written tentative ruling denying the motion to compel arbitration and on January 15, 2013, after oral argument, adopted the tentative ruling as its final order on the motion.[6] The order stated, in pertinent part:

"While defendants are correct that the Fund and the deed of trust investments were made under separate agreements which imposed separate obligations of [*sic*] these defendants, that is not the critical determination. The complaint alleges that the agreements for the Fund and for the individual defendants were performed by the same individuals, Davidson and Mills, who were principals in all three corporations. The allegations state that Davidson and Mills moved investments made with [HDA] in individual deeds of trust to [Fund Co.] as part of the Fund. The determinations of all the

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[6] The trial court also sustained with leave to amend the demurrer by HDA, Davidson, and Mills to several counts based on the statute of limitations. Plaintiffs filed a first amended complaint on January 30, 2013, alleging the same counts and also alleging a tolling agreement.

claims in this action depend on the findings of the actions of Davidson and Mills, individually and in their capacities as principals of the corporations.

"The potential for conflicting rulings can sometimes be avoided by staying either the arbitration or the court action pending resolution of whichever goes first. That does not appear to be a reasonable solution in this case. Here, the claims address both sides of the same transaction. There are claims that defendants improperly took plaintiffs's [*sic*] investments out of individual deeds of trust against [HAD] and that the same deeds of trust were improperly put into the Fund, which raises claims against [Fund Co.] and [Properties]. There could be rulings which would raise factual conflicts—for instance if [HDA] was found not to have taken the deeds of trust from plaintiff, but [Fund Co.] and Properties were found to have put those deeds of trust into the Fund.

"The court is inclined to deny the motion on the grounds that there is a great potential for conflicting rulings if the arbitrable and non-arbitrable claims are tried in separate actions."

4. *Appeal*

Fund Co. and Properties timely appealed the order denying their motion to compel arbitration.[7]

CONTENTIONS

Fund Co. and Properties contend (1) the nonmoving defendants are entitled to enforce the arbitration agreement and therefore are not third parties, as required for

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[7] An order denying a motion to compel arbitration is appealable. (§ 1294.)

section 1281.2, subdivision (c) to apply; (2) the claims against them do not arise out of the same transaction or series of related transactions as the claims against the nonmoving parties, and there is no possibility of conflicting rulings; (3) even if section 1281.2, subdivision (c) applies, the refusal to compel arbitration was an abuse of discretion; and (4) the arbitrator, rather than the trial court, should decide which claims must be arbitrated.

DISCUSSION

1. *Governing Law*

A party to an arbitration agreement can be compelled to arbitrate a dispute that is within the scope of the arbitration agreement. Section 1281.2 states that on a petition filed by a party to a written arbitration agreement, a court must order a party to the agreement to arbitrate a controversy if it finds that an agreement to arbitrate the controversy exists, unless any of three specified exceptions applies. The California Arbitration Act (§ 1280 et seq.) "reflects a 'strong public policy in favor of arbitration as a speedy and relatively inexpensive means of dispute resolution.' [Citation.]" (*Haworth v. Superior Court* (2010) 50 Cal.4th 372, 380.)

Section 1281.2, subdivision (c) states that a court need not order the parties to an arbitration agreement to arbitrate if it determines that "[1] [a] party to the arbitration agreement is also a party to a pending court action or special proceeding with a third party, [2] arising out of the same transaction or series of related transactions and [3] there is a possibility of conflicting rulings on a common issue of law or fact." If the

court so determines, it may refuse to enforce the arbitration agreement and instead order the parties to litigate the dispute in court, among other options. (§ 1281.2, last par.)[8]

Thus, section 1281.2, subdivision (c), the third party litigation exception, allows the trial court to decline to compel arbitration, or stay either the arbitration or pending litigation involving a party to the arbitration and a "third party," in order to avoid conflicting rulings on a common issue of fact or law if the arbitration and the litigation arise from the same transaction or series of related transactions and there is a possibility of conflicting rulings. As used in this provision, the term "third party" means a person who is neither bound by nor entitled to enforce the arbitration agreement. (*Thomas v. Westlake* (2012) 204 Cal.App.4th 605, 612 (*Thomas*); *Laswell v. AG Seal Beach, LLC* (2010) 189 Cal.App.4th 1399, 1407.)

The general rule is that only a party to an arbitration agreement can enforce the agreement. (§ 1281.2; *DMS Services, LLC v. Superior Court* (2012) 205 Cal.App.4th 1346, 1352 (*DMS*); *Jones v. Jacobson* (2011) 195 Cal.App.4th 1, 17.) But there are exceptions to the general rule. One exception provides that a nonparty to an arbitration agreement can enforce the agreement against a party to the agreement if the party

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[8] "If the court determines that a party to the arbitration is also a party to litigation in a pending court action or special proceeding with a third party as set forth under subdivision (c) herein, the court (1) may refuse to enforce the arbitration agreement and may order intervention or joinder of all parties in a single action or special proceeding; (2) may order intervention or joinder as to all or only certain issues; (3) may order arbitration among the parties who have agreed to arbitration and stay the pending court action or special proceeding pending the outcome of the arbitration proceeding; or (4) may stay arbitration pending the outcome of the court action or special proceeding." (§ 1281.2, last par.)

alleges that the nonparty was acting as an agents of a party to the agreement. (*Dryer v. Los Angeles Rams* (1985) 40 Cal.3d 406, 418 ["If, as the complaint alleges, the individual defendants, though not signatories, were acting as agent for the Rams, then they are entitled to the benefit of the arbitration provisions"]; *Thomas, supra,* 204 Cal.App.4th at pp. 614-615 ["a plaintiff's allegations of an agency relationship among defendants is sufficient to allow the alleged agents to invoke the benefit of an arbitration agreement executed by their principal even though the agents are not parties to the agreement"].)

2. *Standard of Review*

We independently review the trial court's interpretation of an arbitration agreement if the interpretation does not depend on the resolution of a factual dispute concerning the credibility of extrinsic evidence. (*DMS, supra,* 205 Cal.App.4th at p. 1352; *Molecular Analytical Systems v. Ciphergen Biosystems, Inc.* (2010) 186 Cal.App.4th 696, 707.) Similarly, whether a nonparty to an arbitration agreement can enforce the agreement is a question of law to the extent that the determination does not depend on the resolution of a factual dispute. (*Thomas, supra*, 204 Cal.App.4th at p. 613; *Molecular, supra*, at p. 708.)

Whether a controversy that is subject to arbitration arises out of the same transaction or series of related transactions as a pending court action or special proceeding is a discretionary decision that we review for abuse of discretion. (*Mercury Ins. Group v. Superior Court* (1998) 19 Cal.4th 332, 349-350; *Birl v. Heritage Care LLC* (2009) 172 Cal.App.4th 1313, 1318-1320.) We also review for abuse of discretion

the trial court's determination that there is a possibility of conflicting rulings on a common issue of law or fact. (*Mercury, supra*, at pp. 349-350; *Metis Development LLC v. Bohacek* (2011) 200 Cal.App.4th 679, 691; *Abaya v. Spanish Ranch I, L.P.* (2010) 189 Cal.App.4th 1490, 1496, 1498; *Henry v. Alcove Investment, Inc.* (1991) 233 Cal.App.3d 94, 101; but see *Acquire II, Ltd. v. Colton Real Estate Group* (2013) 213 Cal.App.4th 959, 972, [stated that the substantial evidence standard applied to the questions whether the claims arose of out a series of related transactions and whether there was a possibility of conflicting rulings].)

3. *The Third Party Litigation Exception Is Inapplicable Because the Nonmoving Defendants Can Enforce the Arbitration Agreements and Therefore Are Not Third Parties*

Plaintiffs allege that the defendants are all related entities and individuals, that each acted as an agent of the others, and that the defendants jointly participated in a scheme to defraud Plaintiffs. They allege that Davidson is president of both HDA and Properties, is the sole shareholder of those entities and of Fund Co., and that "[i]n these capacities" he served as Plaintiffs' investment advisor. They allege that Mills is vice president of HDA and secretary of Properties and was responsible for day-to-day management of the HDA Mortgage Fund.

Plaintiffs allege that HDA advised them to invest in the HDA Mortgage Fund and caused them to exchange some of their investments in loans secured by deeds of trust for shares in the fund. They also allege that HDA, with the assistance of Fund Co., Properties, and the individual defendants, provided them with misleading Portfolio Appraisals misrepresenting the value of their investments in the fund and concealed

numerous loan defaults and foreclosures that impaired the value of their fund investments. Plaintiffs also allege that HDA, Davidson, and Mills provided misleading information and a sham appraisal relating to Desert Hot Springs and, together with the other defendants, arranged to swap the failing investments of other investors in Desert Hot Springs for shares in the HDA Mortgage Fund, to the detriment of the fund. The operation of the HDA Mortgage Fund, governed by the Operating Agreement, is central to Plaintiffs' allegations of fraud and other misconduct.

We conclude that in light of Plaintiffs' allegations that the defendants jointly participated in a fraudulent scheme relating to their investments and in so doing acted as agents of one another, the nonsignatory defendants are entitled to enforce the arbitration agreement in the Operating Agreement. We therefore conclude that the nonsignatory defendants are not third parties within the meaning of section 1281.2, subdivision (c), so the third party litigation exception is inapplicable. In light of our conclusion, we need not decide whether the other statutory requirements are satisfied or whether, having decided that the third party litigation section applied, the trial court properly refused to compel arbitration. The denial of the motion to compel arbitration based on the third party litigation exception was error.

4. *The Trial Court Must Stay This Action in Whole or in Part*

A trial court granting a motion to compel arbitration must, upon a motion by a party to the action, stay the action until the completion of the arbitration. (§ 1281.4.) If the claims subject to arbitration are severable from other claims, the stay may be

limited to the claims subject to arbitration.[9] (*Ibid.*) Having denied the motion to compel arbitration and dismiss or stay the claims against Fund Co. and Properties, the trial court did not address the scope of the required stay. We conclude that the trial court on remand must stay this action in whole or in part.

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[9] The Operating Agreement clearly and unmistakably states that an arbitrator must decide any questions concerning the arbitrability of the dispute, so any questions concerning which claims are subject to arbitration must be decided by an arbitrator, rather than the trial court. (*Dream Theater, Inc. v. Dream Theater* (2004) 124 Cal.App.4th 547, 557.)

DISPOSITION

The order denying the motion to compel arbitration is reversed with directions to the trial court to grant the motion and stay the action in whole or in part. Fund Co. and Properties are entitled to recover their costs on appeal.

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CROSKEY, J.

WE CONCUR:

KLEIN, P. J.

KITCHING, J.