RICHARD PETERSON, et al., Plaintiffs vs. HIGHLAND MUSIC, INC., et al., Defendants.

No. CV 93-4672-WDK

UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

1995 U.S. Dist. LEXIS 22008

June 20, 1995, Decided
June 20, 1995, Filed; June 22, 1995, Entered

LexisNexis(R) Headnotes

COUNSEL: [*1] For RICHARD PETERSON, MIKE MITCHELL, LYNNE EASTON, BARRY CURTIS, plaintiffs: Scott A Edelman, Gibson Dunn & Crutcher, Los Angeles, CA.

For RICHARD PETERSON, MIKE MITCHELL, LYNNE EASTON, NORM SUNDHOLM, BARRY CURTIS, plaintiffs: Evan S Cohen, S Martin Keleti, Cohen & Cohen, Los Angeles, CA.

For RICHARD PETERSON, MIKE MITCHELL, LYNNE EASTON, BARRY CURTIS, plaintiffs: Michael T Whitaker, Lee G Lipscomb, Engstrom Lipscomb & Lack, Los Angeles, CA.

For RICHARD PETERSON, MIKE MITCHELL, LYNNE EASTON, NORM SUNDHOLM, BARRY CURTIS, plaintiffs: Cheryl L Hodgson, Cheryl L Hodgson Law Offices, Santa Monica, CA.

For HIGHLAND MUSIC INC, GUSTO RECORDS INC, G M L INC, defendants: Christopher Chapin, Robert S Besser, Besser & Chapin, Pacific Palisades, CA.

For HIGHLAND MUSIC INC, GUSTO RECORDS INC, G M L INC, defendants: James P Cinque, Cinque & Cinque, New York, NY.

For HIGHLAND MUSIC INC, GUSTO RECORDS INC, G M L INC, defendants: Neal M Goldstein, Goldstein & Ashley, Los Angeles, CA.

JUDGES: William D. Keller, Judge.

OPINIONBY: William D. Keller

OPINION:

MEMORANDUM ORDER

The plaintiffs in this case seek to rescind several recording contracts entered into in the 1960's. After a bench [*2] trial, the matter was taken under submission so that the parties could prepare post-trial briefs in lieu of closing argument. n1

n1 In their post-trial briefs, the parties have addressed several issues (e.g., statute of limitations, adverse possession) on which the Court has already ruled. Except as modified by this Order, the rulings made by the Court at trial shall stand.

FACTUAL BACKGROUND

The plaintiffs are members of a recording group called "The Kingsmen." Beginning in 1963, The Kingsmen entered into a series of recording contracts, pursuant to which 102 recordings (the "Masters") were produced. (Exhibit 48). The Masters are now owned by defendant G.M.L., Inc. ("G.M.L."). According to the plaintiffs, G.M.L. and its predecessors have materially breached the recording contracts. In particular, the plaintiffs claim that the defendants have failed to account and pay royalties. The plaintiffs therefore seek to rescind the recording contracts and recover possession of the Masters.

DISCUSSION

[*3] **A. Choice of Law.**

Federal courts ordinarily apply the choice of law rules of the state in which they sit. See *Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487, 85 L. Ed. 1477, 61 S. Ct. 1020 (1941); Consul Ltd. v. Solide Enterprises, Inc., 802 F.2d 1143, 1146 (9th Cir. 1986).* In deciding choice of law issues generally, the California courts apply a "governmental interest" test. See *Reich v. Purcell, 67 Cal. 2d 551, 63 Cal. Rptr. 31, 432 P.2d 727 (1967); American Bank of Commerce v. Corondoni, 169 Cal. App. 3d 368, 215 Cal. Rptr. 331, 333 (1985); Ashland Chemical Co. v. Provence, 129 Cal. App. 3d 790, 181*

Cal. Rptr. 340, 341 (1982). Where there is a contractual choice of law provision, California courts follow $*S 187 of the Restatement (Second) of Conflict of Laws* (1971). *Nedlloyd Lines B.V. v. Superior Court, 3 Cal. 4th 459, 466, 11 Cal. Rptr. 2d 330, 334, 834 P.2d 1148 (1992).*

This lawsuit has generated considerable confusion among the parties regarding choice of law. Nevertheless, as noted below, the Court finds that the law of the various states implicated by the parties is the same in all aspects relevant to the outcome of this case. Thus, no extensive [*4] choice of law analysis is necessary.

B. The Contracts.

The Masters were recorded pursuant to several contracts. The first four contracts were between The Kingsmen and Jerden Records ("Jerden"), a company owned by Jerry Dennon. (Exhibits 4, 14-16). Under those contracts, The Kingsmen produced recordings for Jerden in exchange for royalties. Jerden, in turn, entered into a series of contracts with Scepter Music, Inc. ("Scepter"), transferring the Masters to Scepter. (Exhibits 1-5). Pursuant to those contracts, Scepter owed Jerden a duty to account and pay royalties. Jerden, in turn, owed a duty to account and pay royalties to The Kingsmen. In 1968, The Kingsmen entered into the last contract at issue here, this time directly with Scepter. (Exhibit 6). This contract required Scepter to account and pay royalties to The Kingsmen.

Pursuant to the foregoing contracts, Scepter took title to the Masters. After a series of sales, the Masters were purchased by defendant G.M.L. As Scepter's successor-in-interest, G.M.L. stands in Scepter's shoes. (R.T., Vol. I, pg. 11:7-9). By an assignment, plaintiffs stand in the shoes of Jerden and Jerry Dennon. (Exhibit 43). Asserting Jerden's [*5] rights, the plaintiffs seek to rescind the contracts through which Jerden transferred its rights to Scepter. (Exhibits 1-5). n2 Asserting their own rights, plaintiffs wish to rescind the 1968 contract, in which the remaining Masters were sold directly to Scepter. (Exhibit 6).

n2 One of those agreements, Exhibit 2, is a contract between Jerden and Scepter, pursuant to which Scepter obtained the rights to "Louie Louie" and "Haunted Castle," two of The Kingsmen's most valuable songs. Defendants have argued that there is no contract between The Kingsmen and Jerden with regard to those songs, and thus there is no contract for plaintiffs to rescind. As noted above, Jerden has assigned its rights to the plaintiffs. (Exhibit 43). Plaintiffs, asserting Jerden's rights, may rescind Exhibit 2, regardless of whether there was any contract between The Kingsmen and Jerden with regard to "Louie Louie" and "Haunted Castle."

C. The Parties.

Some of the original members of The Kingsmen who were parties to the various [*6] recording contracts subsequently left the group, and are not plaintiffs in this action. The defendants argue that these former members are indispensable parties who must be joined under *Fed. R. Civ. P. 19(a)(2)*.

Under the first set of contracts, the rights to the masters flowed from The Kingsmen to Jerden, and from Jerden to Scepter. Scepter owed a duty to account and pay royalties to Jerden, which in turn owed a duty to account and pay royalties to the plaintiffs. Thus, as to the songs recorded under the first set of contracts, plaintiffs are asserting Jerden's rights against G.M.L. As noted above, Dennon and Jerden assigned those rights to the plaintiffs in 1993. (Exhibit 43). n3 As to the 1968 contract, between Scepter and The Kingsmen, all of the members of the group who were parties to the contract are parties to this lawsuit. Thus, they are clearly the proper parties to rescind the contract.

n3 The defendants argue that claims for rescission are not assignable. *Soderberg v. Gens, 652 F. Supp. 560 (N.D.Ill. 1987).* The case cited by the defendants in that regard is a district court case from Illinois, and therefore is not binding. In any event, that case addressed the assignability of the right to rescind a fraudulent securities sale under federal law. As such, it is not persuasive. In California, where plaintiffs brought their claim, a "chose in action," including a right arising out of a contractual obligation, is assignable. See *Cal. Civ. Code § § 954*, 1458.

[*7]

D. Grounds for Rescission.

1. Choice of Law.

As noted above, this lawsuit has generated a great deal of confusion regarding choice of law. As to plaintiffs' grounds for rescission, the parties have focused on New York and California law. n4 This choice of law inquiry is simplified, however, by the fact that the law of California and New York is essentially the same with regard to the grounds for rescission.

n4 In that regard, the Court notes that the most important recording contract, pursuant to which Jerden transferred the rights to "Louie

Louie" and "Haunted Castle" to Scepter, contains a choice of law provision implicating the law of New York. (Exhibit 2, P X). None of the remaining agreements contains a similar provision.

In California, a party may unilaterally rescind a contract if there is a material breach by the other party. *Cal. Civ. Code § 1689(b)(2)*.

> A material breach is one that is so dominant or pervasive as in any real or substantial measure to frustrate the purpose [*8] of the undertaking. If a breach does not go to the root of the matter and can be readily compensated in damages, a party may not rescind.

Fantasy, Inc. v. Fogerty, 984 F.2d 1524, 1530 (9th Cir. 1993) (citations and internal quotations omitted).

Under New York law, a party may rescind where he has suffered "breaches of so material and substantial a nature that they affect the very essence of the contract and serve to defeat the object of the parties." *Affiliated Hosp. Prod., Inc. v. Merdel Game Mfg. Co., 513 F.2d 1183, 1186 (2nd Cir. 1975)*(quoting *Nolan v. Williams Music Co., 300 F. Supp. 1311 (S.D.N.Y. 1969),* aff'd sub nom. *Nolan v. Sam Fox Publishing Company, Inc., 499 F.2d 1394 (2nd Cir. 1974)).* See also *Canfield v. Reynolds, 631 F.2d 169, 178 (2nd Cir. 1980)*(citing Nolan). Rescission is not available where the breach did not go to the "root of the contract." Id.

Given the similarity of the standards for rescission under New York and California law, the result in this case would be the same in either state.

2. Materiality of the Breach.

Pursuant to the relevant contracts (i.e., the contracts by which Scepter obtained the Masters), G.M.L. [*9] and its predecessors owed a duty to account and pay royalties to Jerden (and, in some cases, directly to plaintiffs). At trial, defendants stipulated that no one in G.M.L.'s chain of title made any royalty payments. (R.T., Vol. I, pg. 14:7-8). n5 Defendants also stipulated that there have been numerous uses of the Masters since the 1960's, for which royalties would have been due. (R.T., Vol. I, pp. 12:5-6; 14:23-15:2). Finally, defendants admitted that G.M.L. had not rendered an accounting within the applicable statute of limitations, and that no royalty statements were sent for 30 years. (R.T., Vol. IV, pg. 471:18-25; Vol. II, pg. 74:6-7).

n5 Counsel for the defendants later said: "The fact is no money was paid; it's undisputed. Not a single dime for 30 years." (R.T., Vol. II, pg. 74:2-4).

In light of the stipulated facts, it is clear that there has been a breach sufficient to justify rescission under either New York or California law. G.M.L. and its predecessors had a duty to account and pay royalties; they [*10] had no other duties. Defendants stipulated that royalties were due, no royalties were paid, and no accounting rendered. This amounts to a total breach of the contracts. Such a breach is clearly material enough to justify rescission. Cf. *Nolan v. Sam Fox Publishing Co., Inc., 499 F.2d 1394, 1399 (2nd Cir. 1974)*("An essential objective of a contract between a composer and publisher is the payment of royalties, and a complete failure to pay means this objective has not been achieved."); *Fantasy, Inc. v. Fogerty, 984 F.2d 1524, 1530-31 (9th Cir. 1993)*(no rescission where the defendant paid royalties into an escrow account pending litigation, and kept accurate records of the amounts due). n6

n6 The defendants argue that only $ 270.00 in royalties were actually due. According to the defendants, the failure to pay such a small amount cannot be a "material" breach. This argument misses the point. Because the defendants failed to perform any of their duties under the contracts, the amount of royalties actually due is irrelevant. The total failure of consideration on the part of the defendants frustrated the purpose the contract. Cf. Nolan, supra. This argument also contradicts defendants' position at trial that the failure to account was, by itself, a material breach, even if no royalties were due. (R.T., Vol. II, pp. 81:13-83:7).

[*11]

E. Laches.

1. Choice of Law.

The parties have argued at various times that either New York or California law applies to the defendants' affirmative defense of laches. As with the grounds for rescission, the Court finds that the law of both states is the same.

Under California law, relief based on rescission "shall not be denied because of delay in giving notice of rescission unless such delay has been **substantially** prejudicial to the other party." *Cal. Civ. Code § 1693* (emphasis added); Witkin, Summary of California Law, Contracts § 892, pg. 799 (9th ed. 1987). n7 n7 Defendants argue that the prejudice requirement is part of an alternative test requiring either prejudice or acquiescence in the breach. See *Conti v. Board of Civil Service Commissioners, 1 Cal. 3d 351, 359, 82 Cal. Rptr. 337, 342, 461 P.2d 617 (1969); Asia Investment Co., Ltd. v. Borowski, 133 Cal. App. 3d 832, 838, 184 Cal. Rptr. 317, 322 (1982); Chemical Specialties Manufacturers v. Deukmejian, 227 Cal. App. 3d 663, 672, 278 Cal. Rptr. 128, 134 (1991); County of Fresno v. Fair Employment and Housing Commission, 226 Cal. App. 3d 1541, 1556, 277 Cal. Rptr. 557, 567 (1991).* None of the cases cited by the defendants involves rescission. Rather, those cases discuss laches in different contexts. In spite of the defendants' argument to the contrary, § 1693, which specifically applies to rescission, controls. Cases which discuss laches in different contexts are not applicable.

[*12]

Similarly, New York law requires a defendant claiming laches to prove prejudice as well as delay. See *Airco Alloys Div. v. Niagara Mohawk Power Corp., 76 A.D.2d 68, 82, 430 N.Y.S.2d 179, 187* (4th Dep't 1980)("Laches bars recovery where a plaintiff's inaction has prejudiced the defendant and rendered it inequitable to permit recovery."); *Western Elec. Corp. v. New York City Transit Auth., 735 F. Supp. 1205, 1224 at fn. 20 (S.D.N.Y. 1990).* Thus, the law of both states is the same as to the elements of laches; prejudice as well as delay must be established. n8

n8 The defendants argue that delay creates a presumption of prejudice. The cases cited by the defendants in that regard are inapplicable, because they involve federal rather than state law causes of action. *Jackson v. Axton, 25 F.3d 884 (9th Cir. 1994)* (copyright); *International T. & T. Corp. v. General T. & E. Corp., 518 F.2d 913 (9th Cir. 1975)*(Clayton Act); *Boone v. Mechanical Specialties, 609 F.2d 956 (9th Cir. 1979)*(Title VII); *Lemmon v. Santa Cruz County, Cal., 686 F. Supp. 797 (N.D.Cal. 1988)*(Veterans Reemployment Rights Act). The case at bar, involving a state law contract claim, is not governed by the law of laches relating to federal causes of action.

[*13]

Unlike the California Civil Code, which explicitly requires "substantial prejudice," the New York cases cited by the parties, and those examined by the Court in the course of its own research, to not specify the degree of prejudice necessary to prove laches. Nevertheless, the New York courts repeatedly note that laches is an equitable defense, and that unreasonable delay by the plaintiff bars recovery where such delay "render[s] it inequitable to permit recovery." *Airco, supra 76 A.D.2d at 82, 430 N.Y.S.2d at 187.* If the New York courts were to identify the degree of prejudice needed to prove laches defense, they would certainly require "substantial" prejudice. Insubstantial prejudice is not the kind of prejudice which would "render[] it inequitable to permit recovery." Thus, the Court finds that the law of laches is essentially the same in New York and California.

2. Delay.

At trial, the Court found that plaintiffs delayed unreasonably in bringing their claim for rescission. (R.T., Vol. III, pp. 402:4-403:19). The defendants have therefore established the first prong of their laches defense.

3. Prejudice.

(a) The Value of the Kingsmen Masters. [*14]

G.M.L. obtained the Kingsmen Masters in 1984, when it bought a catalog of over 10,000 recordings from a company called Koala for $ 500,000. (R.T., Vol. IV, pp. 513:17-25; 517:8-19; 519:11-13). Of the approximately 10,000 recordings in the Koala catalog, 200-250 were considered "valuable" by G.M.L. (R.T., Vol. IV, pg. 517:15-19). When asked how many of the Kingsmen Masters would be within the 200-250 "valuable" records, G.M.L.'s vice president, Stephen Kountzman, testified that "Louie Louie" "might" be one of them, but he would not say that all 102 Kingsmen Masters were "valuable." (R.T., Vol. IV, pg. 536:18-22)(emphasis added). In fact, counsel for the defendants asserted that "Louie Louie probably comprises 95 to 98 percent of the income here. The other [Kingsmen] songs didn't generate much money . . . ." (R.T., Vol. IV, pg. 425:18-20). In light of the defendants' testimony and argument, it is clear that of the Kingsmen Masters, only "Louie Louie" had any real value to G.M.L. Assuming that the $ 500,000 purchase price reflects the value of the 200-250 "valuable" masters, the single "valuable" Kingsmen Master accounted for approximately $ 2,000-$ 2,500 of the purchase price, if [*15] the Koala catalog is evaluated on a pro rata basis. n9

n9 This range of figures represents the total purchase price of $ 500,000 divided by the range of "valuable" recordings, 200-250. The Court recognizes the many limitations inherent in this pro rata method of evaluation. For example, it does not take into account potential differences between the 200-250 "valuable recordings," and it ascribes no value at all to the remaining 9,750-9,800 songs. However, lacking any more reliable benchmark, see supra, the Court adopts the pro

> rata evaluation as a rough estimate. The only other alternative is to find that there is not enough evidence regarding the value of the Masters, and that G.M.L. has not met its burden of showing prejudice because it has failed to quantify prejudice with any specificity. In adopting the pro rata approach, rather than simply finding a lack of evidence, therefore, the Court is actually giving the benefit of the doubt to the defendants.

The defendants object to the evaluation of the Masters [*16] on a pro rata basis. (Defendants' Post-Trial Reply Brief, pp. 9-10). However, because the defendants did not produce any other evidence regarding the value of the Kingsmen Masters, nor any of the other recordings, the pro rata approach is the only method of evaluation available. For example, Kountzman testified that the evaluation of the purchase price for the Koala catalog was done "primarily" by Mo Lytle, the owner of G.M.L. (R.T., Vol. IV, pg. 519:15-18). However, the defendants did not produce, by deposition or at trial, any testimony from Mr. Lytle regarding the value of the Kingsmen Masters. Moreover, when asked how G.M.L. arrived at the $ 500,000 purchase price, Kountzman testified that the recordings were not evaluated on an individual basis. (R.T., Vol. IV, pp. 519:19-520:1). Thus, in assessing the value of the Kingsmen Masters, the only evidence before the Court is the overall purchase price of the Koala catalog, the number of masters considered valuable by G.M.L., and the number of Kingsmen Masters considered of value.

(b) The Purchase Price.

Before deciding to purchase the Koala catalog, G.M.L. examined Koala's files to determine whether there were any royalties [*17] due. (R.T., Vol. IV, pp. 514:1-520:9). According to the defendants, the purchase price of the catalog reflected several factors, including the amount of royalties due. (R.T., Vol. IV, pp. 519:15-520:5). After examining the file relating to the Kingsmen Masters, G.M.L. concluded that no royalties were due. (R.T., Vol. IV, pg. 521:2-10). Defendants argue that G.M.L. has suffered prejudice because it purchased the Koala catalog at a price based in part upon its belief that no royalties were due in connection with the Masters.

As noted above, G.M.L. failed to establish that the Kingsmen Masters represented a significant portion of the $ 500,000 purchase price. Indeed, the evidence shows that the Masters reflect only $ 2,000-$ 2,500 of that price. The defendants stipulated that during the four years prior to the lawsuit, G.M.L. received about $ 20,000 in connection with the Kingsmen Masters. (R.T., Vol. IV, pp. 444:23-445:2). Even if this were the only money earned by G.M.L. during ten years of ownership, G.M.L. earned a substantial return for a minimal investment in the Kingsmen Masters. Indeed, under the circumstances, G.M.L. actually benefited from the plaintiffs' delay, because they [*18] were permitted to exploit the Kingsmen Masters without paying royalties. n10 See, e.g., *Field v. Bank of America, 100 Cal. App. 2d 311, 223 P.2d 514 (1950)*(in an action to annul a trust, trustee was not prejudiced, but actually benefitted from the delay, because fees accrued for many years).

> n10 G.M.L. will not be deprived of these profits in any future proceeding. Any new claim by the plaintiffs against G.M.L. for past royalties would be barred by claim preclusion. See *Fund for Animals, Inc. v. Lujan, 962 F.2d 1391, 1398 (9th Cir. 1992)* (claim preclusion bars the assertion of any theory of recovery that could have been asserted in the first action).

Even if G.M.L. had established prejudice, such prejudice must be a result of the plaintiffs' delay in order to support the laches defense. See *Cal. Civ. Code § 1693* (relief "shall not be denied because of delay in giving notice of rescission unless **such delay** has been substantially prejudicial to the other party."); *Airco, supra, 76 A.D.2d at* [*19] *82* ("Laches bars recovery where **a plaintiff's inaction** has prejudiced the defendant and rendered it inequitable to permit recovery."). In the case at bar, any prejudice to G.M.L. was caused as much by its own negligence as it was the plaintiffs' delay. Such negligence should be balanced against the prejudice asserted by G.M.L. See, e.g., *Merchant v. Lymon, 828 F. Supp. 1048, 1063 (S.D.N.Y. 1993)*(prejudice is counterbalanced by culpability of the defendant in creating the circumstances causing the prejudice).

As noted above, G.M.L. examined the seller's files before purchasing the Koala catalog. The Kingsmen file contained all of the relevant recording contracts, which provided that royalties were owed either to Jerden Records or to The Kingsmen. Nothing in the file indicated that the potential royalty recipients had been bought out, or were otherwise not entitled to royalties. G.M.L., recognizing the importance of determining whether any royalties were due, allegedly tried to locate Jerden, but was unsuccessful. According to Mr. Kountzman, G.M.L. ran a Dun & Bradstreet report, called directory assistance in Seattle, and inquired with either the Secretary of State or Attorney [*20] General of Washington State. (R.T., Vol. IV, pg. 516:13-23).

When asked by the Court whether there was a written record of G.M.L.'s inquiry into the potential royalty obligations attached to the Kingsmen Masters, Mr. Kountzman testified that notes were kept at the time, and that he recently had reviewed the Kingsmen file. (R.T., Vol. IV, pp. 518:6-519:1). In spite of the specific inquiry from the Court, however, G.M.L. failed to produce either the notes or the file. Moreover, defendants failed to produce Mo Lytle, who was primarily responsible for putting together the Koala purchase. G.M.L. thus produced very little evidence of its attempt to locate Jerden. Given this lack of evidence, and an obvious incentive not to find any potential royalty claimants, the Court is not convinced that such efforts were made.

However, even if they were, there is no evidence at all that G.M.L. attempted to locate Jerry Dennon, who signed the contracts on behalf of Jerden, and there is no evidence that G.M.L. attempted to locate The Kingsmen. If G.M.L. had conducted a more thorough investigation, it could have found Dennon and/or The Kingsmen, and would have known that royalties were due on the Kingsmen [*21] Masters. n11 G.M.L., which specializes in obtaining master recordings without royalty obligations attached, should know how to determine whether royalties are owed on a given master, and should know how to prove that reasonable efforts were made to make such a determination. (See R.T., Vol. IV, pp. 512:19-513:16). Despite its experience, G.M.L. failed to produce evidence of a reasonable investigation.

n11 For example, Dennon testified that he was listed in the Seattle phone book during the 1970's and 1980's. (R.T., Vol. III, pg. 330:11-17). When asked by the Court, Kountzman testified that he remembered Jerry Dennon's name from the contracts, but that he did not try to contact Dennon personally, and could not provide a reason for failing to do so. (R.T., Vol. IV, pp. 545:7-546:15). As for The Kingsmen, the group began performing again in the early 1980's, and continued throughout the decade. (R.T., Vol. IV, pp. 582:10-586:12). If G.M.L.'s investigation had been reasonably thorough, G.M.L. could have located both Dennon and The Kingsmen.

[*22]

Because the investigation was inadequate, G.M.L. could not reasonably assume that the Kingsmen Masters were unencumbered by any royalty obligations, and any prejudice resulting from that assumption was caused as much by the defendants' negligence as it was by the plaintiffs' delay.

(c) The Re-Recordings.

When G.M.L. purchased the Masters, G.M.L. already owned a re-recording of three Kingsmen songs, including "Louie Louie." This re-recording was performed by two of the original members of The Kingsmen, including the lead singer. (R.T., Vol. IV, pp. 520:5-9; 522:5-523:3; 525:5-526:5; 529:1-4). Stephen Kountzman testified that because G.M.L. owned the re-recordings, G.M.L. probably would not have purchased the original Masters if there had been royalty obligations attached. Id.

Assuming that G.M.L. would not have purchased the Masters if it had known that royalties were due, the only prejudice to G.M.L. would be the portion of the purchase price attributable to the Kingsmen Masters. However, as noted above, the Kingsmen Masters represented just a fraction of the purchase price, from which G.M.L. has earned a substantial return. Moreover, G.M.L. still owns the re-recordings. [*23] If the plaintiffs were to recover the Masters, G.M.L. would be in the same position as it was before, except for the profits earned during the years of its ownership. Therefore, G.M.L. has not established anything approaching substantial prejudice.

(d) Marketing Efforts.

Believing that no royalty payments were due, both G.M.L. and Highland undertook some efforts to market the Masters. (R.T., Vol. IV, pp. 526:24-527:22; 557:14-558:23). The defendants argue that they would suffer prejudice if the plaintiffs were permitted to rescind. As the Court noted at trial, the evidence of marketing efforts was slim. n12 Thus, the defendants have failed to produce evidence of any substantial prejudice resulting from the marketing efforts.

n12 See statement by the Court at R.T., Vol. IV, pg. 581:20-22: "I, frankly, have heard very little effort on their part, very little testimony regarding effort by the defense to merchandise these materials. Very little."

(e) Pricing.

In an attempt to establish prejudice, [*24] the defendants offered the testimony of Mr. Stephen Hawkins, president of Highland Music, Inc. ("Highland"). (R.T., Vol. IV, pg. 459:5-6). Highland, which was initially a defendant in this case, holds an exclusive license from G.M.L. in connection with the Kingsmen Masters. (R.T., Vol. IV, pg. 460:23). Pursuant to that license, Highland marketed the Kingsmen Masters. Highland's decisions in pricing its products were based in part upon its assumption that no royalties were due. (R.T., Vol. IV, pp. 553:1-557:5). In light of Highland's low profit margin, even a small royalty obligation would be significant in it's decision-making process. (R.T., Vol. IV, pg. 571:16-25). According to the defendants, Highland's reliance upon the lack of royalty obligation in pricing its products establishes prejudice sufficient to sustain their laches defense.

To begin with, it is doubtful that prejudice to Highland constitutes a defense for G.M.L. Although Highland was initially a defendant, the action against Highland was stayed when Highland filed for bankruptcy protection. More importantly, G.M.L., rather than Highland, owns the Masters and is Scepter's successor-in-interest. (R.T., Vol. I, pg. 11:7-9). [*25] Plaintiffs are attempting to recover the Masters from G.M.L., not Highland.

Laches, however, requires prejudice to the other party, not some third party. See *Cal. Civ. Code § 1693* (substantial prejudice to "the other party" required); *Airco, supra, 76 A.D.2d at 82, 430 N.Y.S.2d at 187* ("Laches bars recovery where a plaintiff's inaction has prejudiced **the defendant** and rendered it inequitable to permit recovery.")(emphasis added). Therefore, any purported prejudice to Highland is not relevant to G.M.L.'s laches defense.

Of course, one might argue that G.M.L. could not have licensed the Masters if there had been royalties due because Highland would not have licensed them from G.M.L., given Highland's low profit margin. However, G.M.L. did not make that argument, and did not offer any evidence that it could not have licensed the Kingsmen Masters to someone else.

In any event, even if prejudice to Highland somehow affects G.M.L., the Court does not perceive any prejudice resulting from Highland's pricing decisions. If the plaintiffs were seeking to recover past royalties, the prejudice to Highland would be clear. However, because the plaintiffs seek only to rescind, Highland's [*26] pricing decisions are irrelevant. Highland marketed the Masters and charged a price that did not account for royalties. Highland did not pay any royalties on those sales, and is not now being asked to do so. Therefore, Highland will retain all of the profits which it expected to make when it priced the products. Under the circumstances, Highland will not suffer any prejudice as a result of its pricing decisions. n13

n13 To the extent that it purchased an exclusive license from G.M.L., Highland could argue that it will suffer prejudice because the price of the license reflected Highland's belief that royalties were not due. Unlike the pricing decisions, this kind of prejudice would extend to sales that Highland expected to make in the future. However, the defendants did not offer any evidence as to the price of the license from G.M.L., and did not argue that Highland would suffer prejudice on this basis. Therefore, the defendants have not established such prejudice.

(f) Defense Prejudice.

The defendants [*27] also claim to be prejudiced because the passage of time has deprived them of evidence necessary to defend the case. In that regard, the defendants point out that "royalty statements which may have been rendered from Scepter to Jerden and from Jerden to The Kingsmen have all been lost." (Post-Trial Memorandum, pg. 37). According to the defendants, such statements might have shown that the Kingsmen Masters were "unrecouped," and thus no royalties due to the plaintiffs. n14 The defendants argue that they could have defeated the rescission claim by proving that, because no royalties were due, there was no material breach.

n14 Under the recording contracts, the costs of producing and promoting the Masters were advanced by the record companies. Until the advance costs were recovered, the Masters were "unrecouped" and the plaintiffs were not entitled to any royalties.

At trial, however, the defendants stipulated that no royalty statements were ever sent to the plaintiffs. (R.T., Vol. II, pg. 74:6-7). Moreover, defendants [*28] argued that the failure to account alone was a material breach, even if no royalties were due. (R.T., Vol. II, pp. 81:13-83:7). They cannot now argue defense prejudice resulting from the loss of royalty statements "which may have been rendered." By their own admissions, there were no statements, and the amount of royalties due is irrelevant to the materiality of the breach.

CONCLUSION

For the foregoing reasons, the Court finds that the plaintiffs are entitled to rescind the recording contracts. Thus, plaintiffs may recover possession of the Masters.

IT IS SO ORDERED.

Dated: 6/20/95

Judge William D. Keller