SEGA OF AMERICA, INC., Legal Department Attorney-Client Communication Privileged and Confidential

To: From:	Tom Klitgaard	cc:	Paul Rioux Shinobu Toyoda Mike Ribero Michealene Cristini Risley
Subject:	DIC- Lawsuit by Sega on Network Series		
Date:	September 25, 1995		

Attached is a draft complaint against DIC on the network agreement. Michealene has had further discussions with DIC last week and needs until the end of this week to bring the negotiations to a conclusion, if possible.

The complaint is based upon the September, 1992, letter of intent (copy attached) for the network series and syndication series. Andy Heyward contends that the only agreements for the network series were an agreement dated October 29, 1991 (copy attached) and the September 1992 letter of intent. Sega claims that the 1991 agreement was terminated by the letter of intent, and that the parties did not thereafter ever reach a final agreement, thus leaving the letter of intent the operative document.

The letter of intent is very brief as to the network series. It simply provides that "A special has been already ordered by ABC and DIC shall continue to act as Sega's agent for the negotiation of a network weekly series. If an agreement is entered into with the network, DIC will have the exclusive right to produce the series."

The letter of intent provides that Sega shall retain ownership and copyrights of existing characters and any new characters or elements developed in "any" animation productions. However, it is unlcear whether this retention of rights pertains to the network series, the syndication series, or both. Further, the same ambiguity exists as to (a) the obligations of the parties to refund all monies paid by Sega, less reasonable expenses incurred in production, distribution or promotion of the "series," and (b) the treatment of all work performed on the "series" as work made for hire and as the sole property of Sega, in the event the letter of intent is terminated.

The letter of intent provided that the parties would use their best efforts to negotiate in good faith to reach a mutual understanding concerning the terms of a formal agreement within 30 days of the date of execution. The complaint alleges that a final agreement was never executed and asks for a declaration of rights of the parties, together with an accounting by DIC of monies recieved by it as Sega's agent for the network series. The court would permit DIC to deduct its expenses as an agent, but these expenses would need to be audited as part of the court proceedings.

The complaint will probably not produce an immediate amount of substantial funds, apart from what may be recovered on the accounting (which is as yet undetermined). However, the complaint would seek to establish clearly Sega's exclusive right to revenues from the use of its copyrights and characters in broadcasts of the network programs on foreign television, reruns on domestic network television, and on cable programs. Additionally, the complaint would seek to establish Sega's exclusive rights to the music and the cels for the network programs. Finally, the complaint would seek to establish Sega's portion of the revenues from the home video sales and its rights and to its prevent sales of cels. Most importantly, the complaint would seek to protect Sega's copyrights and characters from use by DIC in any future network programming.

The Mitchell Silberberg firm, which prepared the complaint, estimates that the cost of the suit through trial would be in the range of \$475,000- \$781,000. I beleive this figure is too low, in view of the fact-intensive nature of the dispute. I would increase the estimate by roughly 50%, to \$900,000- \$1,200,000, depending upon the extent of discovery and the intensity with which DIC would defend.

I look forward to discussing the complaint and our strategy with you.

Attachments

- A. Draft Complaint for Declaratory Relief against DIC Enterprises.
- B. Letter Agreement dated September 23, 1992
- C. Letter Agreement dated October 29, 1991

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	z	11377 West Olympic Boulevard Los Angeles, California 90064-1683	DRAFT	I	
	3	(310) 312-2000			
	4	Attorneys for Plaintiff Sega of America, Inc.			
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	7		CHARLEN OF CHIRDINE		
	8	SUPERIOR COURT OF THE STATE OF CALIFORNIA			
	9	FOR THE COUNTY	OF LOS ANGELES		
	10		0400 X (0		
	11	SEGA OF AMERICA, INC.,	CASE NO.	8 DD 2 ⁻¹¹ 1/612 2	
	12	Plaintiff,	COMPLAINT FOR DECLARA RELIEF, BREACH OF FIDUCI	IARY	
	13	V.	DUTY, VIOLATIONS OF CALIFORN BUSINESS AND PROFESSIONS CO		3
	14	DIC ENTERPRISES, INC. and DOES 1 through 10, inclusive,	§17200, CONVERSION, AND ACCOUNTING AND IMPOS A CONSTRUCTIVE TRUST	TTION OF	7
	15	Defendants.	A CONSTRUCTIVE TROOT		
	16)		
	17	Multiple Carp of America Inc.	Charles Inc. (Court) allowers		
	18	Plaintiff Sega of America, Inc. ("Sega") alleges:			
	19	ALLEGATIONS COMMON TO ALL CAUSES OF ACTION			
	20	ALLEGATIONS COMMON TO ALL CRUSES OF ACTION			
	21	1 Same is a corporation incorport	ated in the State of California, wit	th its	
	22 23	1. Sega is a corporation incorporated in the State of California, with its principal place of business in Redwood City in the County of San Francisco, California.			
	24 25	2. Sega is informed and believes,	and upon such information and	belief	
	26	alleges, that defendant DIC Enterprises, Inc. ("DIC") is a corporation incorporated in the		a	
	27	State of California, and is a wholly-owned subsidiary of DIC Animation City, Inc. DIC			
	28	has its principal place of business in the City			
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Sega is presently unaware of the identities of Defendants sued as Does 1 3. through 10, and thereby sues said Defendants by such fictitious names. Sega will seek leave of court to amend this complaint to set forth their true identities when ascertained. Sega is informed and believes, and upon such information and belief alleges, that said Defendants were actively involved in or participated in the actions hereinafter alleged, and are liable to Sega therefor.

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On or about October 29, 1991, Sega and DIC Animation City, Inc. entered 8 4. into a written agreement (the "1991 Agreement") pursuant to which DIC proposed to acquire from Sega certain rights to produce, distribute and exploit live action and 10 animated television programming based upon Sega's video game program "Sonic the 11 Hedgehog". A true and correct copy of the 1991 Agreement is attached hereto marked 12 Exhibit A, and is incorporated herein by reference. 13

Under the 1991 Agreement, if DIC failed to obtain a network commitment 15 5. or syndication order by May 1, 1992, the 1991 Agreement became terminable by either 16 party. DIC in fact failed to obtain a network commitment or syndication order by 17 May 1, 1992, at which time the 1991 Agreement became terminable. 18

On or about September 24, 1992, Sega, DIC, and another entity, Bohbot 6. Communications, Inc. entered into a new agreement (the "1992 Agreement") which superseded the 1991 Agreement. A true and correct copy of the 1992 Agreement is 22 attached hereto marked Exhibit B, and is incorporated herein by reference. 23

The 1992 Agreement contemplated that the parties would use their best 25 7. efforts and "negotiate in good faith to reach a mutual understanding concerning the 26terms of the formal agreement within 30 days of the date on which all parties execute 27 this letter." Exh. B, Page Four. Following the execution of the 1992 Agreement, the 28

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parties in fact entered into prolonged negotiations over several years to that end, which negotiations were unsuccessful. [The last complete version of a draft formal agreement was prepared by counsel for Sega as of September 21, 1994 ("1994 Draff"). A true and correct copy of the 1994 Draft is attached hereto marked Exhibit C.]

Notwithstanding that the parties never signed a more formal or different 8. agreement following the execution of the 1992 Agreement, DIC proceeded to produce 26 episodes of the Network Series, comprising the pilot and 25 subsequent episodes, which episodes have been broadcast on the ABC television network.

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On or about July 20, 1995, DIC's President, Andy Heyward, confirmed in 9. 11 writing in a letter directed to Sega that the only agreements that had ever existed 12 between Sega and DIC in DIC's view were the 1991 Agreement and the 1992 13 Agreement. (A true and correct copy of that letter is attached hereto marked Exhibit 14 D. Further recognizing that Sega and DIC had failed to reach any agreement 15 superseding the 1992 Agreement, on September 6, 1995, DIC's counsel directed a 16 letter to counsel for Sega proposing still further negotiations on a range of issues 17 relating, inter alia, to the Network Series. A true and correct copy of that letter is 18 19 attached hereio marked Exhibit E.]

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Under the 1992 Agreement, Sega retains "all ownership and copyrights in 10. 21 existing characters and any new characters or elements created for any animation 22 productions. In addition, Sega shall have the right to use any animation produced in 23 future version (sic) of its video games on a royalty-free basis." Exhibit B, Page Two.

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Under and by virtue of the 1992 Agreement, DIC was to act as Sega's 11. agent for the negotiation of a network weekly series (hereinafter the "Network Series"), and in the event an agreement was entered into with ABC, DIC was to have the

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exclusive right to produce the series. Exhibit B, Page One. As Sega's agent, and by reason of the trust and confidence that Sega thereby reposed in DIC and that DIC 2 assumed from Sega, DIC had and maintained at all times mentioned herein a fiduciary 3 4 relationship with Sega.

Sega is informed and believes, and upon such information and belief 12. 6 alleges, that at the time it was acting as Sega's agent and fiduciary in negotiations with 7 ABC, 80% of the stock of DIC had been acquired or was in the process of being 8 acquired by ABC. Sega is further informed and believes, and upon such information 9 and belief alleges, that DIC ultimately entered into a network licensing agreement with 10 ABC pursuant to which DIC would produce and ABC would broadcast the Network 11 Series, and in so doing had a duty not only to negotiate at arms length with ABC but 12 to act in Sega's best interests. Sega is informed and believes, and upon such 13 information and belief alleges, that notwithstanding the foregoing, DIC failed to act in 14 Sega's best interests because, among other reasons, DIC has at all times mentioned 15 herein failed and refused to account to Sega with respect to the expenses incurred in 16 producing or distributing the Network Series and with respect to any and all monies 17 obtained or received by DIC in connection with the Network Series. 18

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FIRST CAUSE OF ACTION FOR DECLARATORY RELIEF

Sega incorporates by reference as though fully set forth hereunder the 13. allegations of paragraphs 1 through 11 inclusive hereof.

An actual controversy has arisen and now exists between Sega and DIC in 14. that Sega contends that:

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1	A. The 1991 Agreement expired according to its terms, and by virtue of	
2	their execution of the 1992 Agreement, DIC and Sega effected a novation, intending to	
3	extinguish any obligations that may have existed between them under the 1991	
4	Agreement and substituting for any such old obligations the new obligations created by	
5	the 1992 Agreement.	
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7	B. The 1992 Agreement is subject to termination by Sega at this time	
8	for the following independent reasons, among others:	
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10	(i) the parties have failed to reach agreement on material terms	
11	and conditions of any different or more formal agreement between and among them;	
12		
13	(ii) DIC has violated its fiduciary duties to Sega; and	
14		
15	(iii) DIC has otherwise breached the 1992 Agreement.	
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17	C. As of the filing of this complaint and consequent termination of the	
18	1992 Agreement by Sega, DIC has no rights whatsoever with respect to further	
19	production, distribution, or exploitation of the Network Series, all rights in or to which,	
20	including but not limited to all ownership and copyrights in existing characters and any	
21	new characters or elements created for any animation productions by DIC, belong	
22	solely and exclusively to Sega;	
23		
24	D. As Sega's agent, DIC is obliged to account to Sega for all monies	
25	purportedly expended or received by DIC heretofore and hereafter in connection with	
26	the Network Series.	
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28	15. DIC disputes some or all of Sega's contentions.	
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A declaration by the court is necessary at this time because DIC and Sega 16. 1 have been unable to agree with respect to the matters in controversy, and in order to \mathbf{z} avoid a continuing and accelerating dispute across a multiplicity of issues, likely to 3 produce a multiplicity of actions. Sega has no other plain, speedy or adequate remedy 4 5 at law. 6 SECOND CAUSE OF ACTION FOR BREACH OF FIDUCIARY DUTY 7 8 Sega incorporates herein by reference as though fully set forth hereunder 17. 9 the allegations of paragraphs 1 through 11 inclusive hereof. 10 11 The actions of DIC alleged above constitute breaches of the fiduciary duty 18. 12 13 owed by DIC to Sega. 14 As a direct and proximate result of DIC's breaches of its fiduciary duty to 15 19. Sega, Sega has suffered damages in an amount not now known, but which exceeds the 16 jurisdictional limit of this court. Sega will seek leave of court to amend its complaint to 17 set forth the exact amount when ascertained. 18 19 In doing the aforementioned acts, DIC was guilty of malice, fraud, and 20. 20oppression. By reason thereof, Sega is entitled to recover from DIC in addition to its 21 actual damages, damages for the sake of example and by way of punishing DIC in an 22amount according to proof. 23 24Unless preliminarily and permanently enjoined from so doing, DIC will 21. 25continue to exercise or to purport to exercise rights with respect to the production, 26 distribution, marketing and other exploitation of the Network Series, its artwork, 27 characters and other elements, and cels and other items embodying the foregoing, all of 28

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r	which rights belong to Sega. Sega has no remedy at law adequate to address DIC's
2	actions, and while DIC's actions have caused, are causing and will continue to cause
3	injury to Sega, its damages are irreparable, irremediable, and not calculable in monetary
4	terms.
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6	THIRD CAUSE OF ACTION FOR VIOLATIONS OF
7	CALIFORNIA BUSINESS AND PROFESSIONS CODE §17200 ET SEQ.
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9	22. Sega incorporates herein by reference as though fully set forth hereunder
10	the allegations of paragraphs 1 through 11 inclusive hereof.
11	
12	23. The acts of DIC alleged above constitute unfair competition and unfair
13	acts and practices prohibited by California Business & Professions Code §17200.
14	
15	24. Sega is informed and believes, and upon such information and belief
16	alleges, that as a direct and proximate result of its unfair competition alleged above,
17	DIC has received and will receive money, property and other benefits that rightfully
18	belong to Sega, and Sega is entitled to appropriate orders of this court restoring all such
19	money, property and other benefits to Sega.
20	
21	25. DIC's continuing acts and conduct are causing and threaten to continue to
22	cause Sega irreparable and irremediable injury not readily calculable in money
23	damages, and by reason thereof Sega is entitled to an order preliminarily and
24	permanently enjoining DIC from engaging in such acts and conduct, as prayed for
25	below.
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	FOURTH CAUSE OF ACTION FOR CONVERSION
	Sega incorporates herein by reference as though fully set forth hereunder s of paragraphs 1 through 11 inclusive hereor.
the owner, an	At all times herein mentioned since their creation, Sega was, and still is, Id was, and still is, entitled to the possession of the following personal
property, nam	nely the original cels created in the course of production of the Network
Series;	
alleges, that	Sega is informed and believes, and upon such information and belief in or about January, 1994, the cels created in the course of production of Series were delivered to DIC.
29.	Sega is informed and believes that at the time the cels were delivered to
DIC, they had	d varying values in the resale market, in amounts not presently known to
-	ill seek leave of the court to set forth the exact values when ascertained.
	Sega is informed and believes, and upon such information and belief commencing in or about January, 1994 and continuing thereafter, without

19 out 20 all Sega's consent, DIC has sold a number of the Network Series cels, and is continuing to 21 sell Network Series cels, to persons and entities the identities of whom or which are 22 presently unknown to Sega, and thereby converted those Network Series cels and the 23 proceeds of their sale to its own use. 24

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Between the time of DIC's conversion of the Network Series cels and the 30. commencement of this action, Sega and its employees and attorneys have properly expended substantial time and money in pursuit of the converted cels, all to Sega's 28

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further damage in an amount not yet ascertained. Sega will seek leave of court to 1 amend this complaint to set forth the exact sum when ascertained. 2 3 In doing the aforementioned acts, DIC was guilty of malice, fraud, and 31. $\overline{4}$ oppression. By reason thereof, Sega is entitled to recover from DIC in addition to its 5 actual damages, damages for the sake of example and by way of punishing DIC in an 6 7 amount according to proof. 8 9

FOURTH CAUSE OF ACTION FOR ACCOUNTING AND IMPOSITION OF A CONSTRUCTIVE TRUST

32. Sega incorporates herein by reference as though fully set forth hereunder the allegations of paragraphs 1 through 11, 17, and 25 through 28 inclusive hereof.

33. In addition to the foregoing, between the date of execution of the 1992
Agreement and the commencement of this action, DIC has collected monies under and
by virtue of that agreement, the amount of which is not known to Sega.

34. On an accounting by DIC, there will be found a balance due to Sega, the
amount of which is not known to Sega. An accounting by DIC is necessary to show
and would in fact show that amount.

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35. Prior to the commencement of this action, Sega demanded an accounting
for DIC's expenses and revenues in connection with DIC's actions pursuant to the 1992
Agreement. DIC has never rendered such an accounting to Sega, nor paid to Sega any
money DIC was obligated to pay to Sega thereunder.

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1	36. By virtue of DIC's violation of the relationship of trust and confidence		
2	that has existed at all times mentioned herein by reason of DIC's status as Sega's agent		
3	under the 1992 Agreement, DIC holds all money, property and other benefits it has		
4	received or may hereafter receive under, in connection with, as a result of or arising		
5	from the 1992 Agreement as a constructive trustee for Sega's benefit.		
6			
7	WHEREFORE, Sega prays:		
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9	1. Under its First Cause of Action, for an order declaring that its contentions		
10	are correct;		
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12	2. Under its Second and Fourth Causes of Action, for its actual damages,		
13	according to proof;		
14	and the second sec		
15	3. Under its Third Cause of Action, for restitution in an amount according to		
16	proof;		
17	The second mind Termine and Diffle Courses of Action for an		
18	4. Under its Second, Third, Fourth and Fifth Causes of Action, for an		
19	accounting of all monies owing to Sega;		
20	5. Under its Second, Third, Fourth and Fifth Causes of Action, for an order		
21	5. Under its Second, Third, Fourth and Firth Causes of Action, for all order declaring that DIC holds all money, property and other benefits it has received under,		
22	in connection with, as a result of or arising from the 1992 Agreement in trust for Sega;		
23	in connection with, as a result of or ansing from the 2000 figure and a second of the		
24 25	6. Under its Fourth Cause of Action, for its costs, including attorneys' fees,		
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Under its Fourth Cause of Action, for punitive damages in an amount 1 7. 2 according to proof at mial; 3 Under its Second and Third Causes of Action, for a preliminary and 8. 4 permanent injunction enjoining DIC and all those acting in concert or participating 5 with DIC from: 6 7 Taking any action to produce any additional episodes of the 8 A. 9 Network Series; 10 Granting or purporting to grant any rights with respect to the B. 11 Network Series or any character or element therein, including but not limited to any 12 rights to air the Network Series on cable television, whether on the USA Network or 13 14 otherwise; 15 Distributing or attempting to distribute the Network Series in any C. 16 media worldwide, including but not limited to non-U.S. television and home video 17 markets; 18 Retaining or selling any original cels from the Network Series; or D. 19 20 Asserting to any other person or entity, aside from pleadings in a E. 21 legal action, that it has any right, title and ownership in and to any characters or 22 elements in the Network Series, including but not limited to any new characters or 23 elements created by DIC in connection with the production of the Network Series; 24 25 For its costs of suit incurred herein; and 9. 26 27 28 hall. Silbarberg a 11 09-18-95 12:03PM P022 #33 310+312+3789

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1	10. For such other and fu	rther relief as the court deems appropriate.
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З	Dated: September 1995	MITCHELL, SILBERBERG & KNUPP ROY L. SHULTS
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6		Roy L. Shulis
7		Attorneys for Plaintiff Sega of America, Inc.
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