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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

WALLACE B. BROWN et al.,

Plaintiffs and Respondents,

v.

DAVID A. COLTON et al.,

Defendants and Appellants.

G046240

(Super. Ct. No. 30-2011-00477186)

O P I N I O N

Appeal from an order of the Superior Court of Orange County, Nancy Wieben Stock, Judge. Affirmed in part, reversed in part, and remanded.

Waldron & Bragg, Gary A. Waldron, Jacob C. Gonzales and Corbett H. Williams for Defendants and Appellants.

Law Offices of Roland C. Colton, Roland C. Colton and James E. Pollock for Plaintiffs and Respondents.

* * *

Plaintiffs and respondents¹ invested in three investment funds defendants and appellants² created over a six-year period to purchase and manage three portfolios of commercial real estate. Each fund was separate from the other funds and presented two distinct investment options. Investors could become a member in the entity Defendants formed to take title to the entire portfolio or investors could purchase a fractional ownership interest in a specific property included in the portfolio without becoming a member in the entity. Some Plaintiffs became members in one or more of the investment funds, some became joint owners of one or more individual properties, and some did both.

Defendants filed two motions to compel different groups of Plaintiffs to arbitrate their claims relating to these investments. The first motion sought to compel Plaintiffs who purchased an ownership interest in a specific property to arbitrate their claims. Defendants argue their agreement with these Plaintiffs incorporated the arbitration provision from another document, but the contractual language does not support Defendants' argument. We therefore affirm the trial court's decision denying

¹ Plaintiffs and respondents are Wallace B. Brown, individually and as Trustee of the Wallace B. Brown DDS, PC, Profit Sharing and Money Purchase Plan & Trust, Patricia L. Brown, Andrew B. Christensen, Mary T. Christensen, Michael G. Davis Properties, LC, Robert H. Davis Properties, LC, Sally Davis, Mary DeRose, as Trustee of the DeRose Living Trust, Ezekiel Dumke III, Sabio Investments, Ltd., Sabio Investments, LLC, Joseph A. Infelise and Lila Jane Infelise, as Trustees of the Joseph A. Infelise and Lila Jane Infelise 2005 Declaration of Trust, Patrick B. Quast and Joan C. Quast, as Trustees of the Patrick B. Quast and Joan C. Quast 2003 Declaration of Trust, and John S. Young. We collectively refer to all plaintiffs and respondents as Plaintiffs.

² Defendants and appellants are David A. Colton, individually and as Trustee of the Colton Family Trust, Linda Colton, Jon W. McClintock, Colton Real Estate Group, Colton Capital Corporation, and Colton Properties, Inc. We collectively refer to Colton Real Estate Group, Colton Capital Corporation, and Colton Properties, Inc. as the Colton Entities, David A. Colton and Linda Colton as the Coltons, and all defendants and appellants as Defendants.

this motion because Defendants failed to establish they entered into an arbitration agreement with these Plaintiffs.

The second motion sought to compel Plaintiffs who purchased membership interests in any of the three investment funds to arbitrate their claims. Based on Code of Civil Procedure section 1281.2, subdivision (c),³ the trial court denied this motion because the court concluded requiring some Plaintiffs to pursue their claims in an arbitral forum while others pursued their claims in a judicial forum would be inefficient and could lead to conflicting rulings.

Section 1281.2(c) grants a trial court discretion to refuse to enforce a written arbitration agreement when (1) a party to the agreement also is a party to pending litigation with a third party who did not agree to arbitration; (2) the pending third party litigation arises out of the same transaction or series of related transactions as the claims subject to arbitration; and (3) the possibility of conflicting rulings on common factual or legal issues exists. A trial court has no discretion to deny arbitration under section 1281.2(c) unless all three of these conditions are satisfied.

Because Defendants failed to request a statement of decision, we must presume the trial court found section 1281.2(c)'s conditions were satisfied for all Plaintiffs who purchased a membership interest in one or more of the three investment funds. We nonetheless reverse the trial court's ruling because the record lacks substantial evidence to support the implied finding that each of section 1281.2(c)'s conditions was satisfied for any of these Plaintiffs. We remand the matter for the court to consider the motion under section 1281.2(c) as it applies to investors in each fund. As explained below, the possibility exists that some groups of Plaintiffs may satisfy section 1281.2(c)'s conditions, but we cannot make that determination on the current record.

³ All statutory references are to the Code of Civil Procedure. For convenience, we will refer to section 1281.2, subdivision (c), as section 1281.2(c).

I

FACTS AND PROCEDURAL HISTORY

The Colton Entities are in the business of purchasing and managing commercial real property. They create separate “funds,” formed as either limited partnerships or limited liability companies, to solicit investors and take title to each portfolio of commercial office buildings they purchase. One of the Colton Entities serves as the general partner or managing member for each fund and manages the portfolio of properties the fund holds. The Coltons and McClintock are directors, officers, and shareholders of the Colton Entities.

Each fund the Colton Entities created had two types of investors. “Share investors” purchased an interest in the fund itself and became either limited partners or members depending on whether the fund was formed as a limited partnership or a limited liability company. Share investors did not hold title to any of the commercial properties held in the fund, but rather held a passive ownership interest in the entity that held title. “Tenant in common investors” purchased a tenant-in-common interest in one or more of the commercial properties that made up the fund. Tenant-in-common investors held an ownership interest in a specific property or properties along with the fund itself, but had no right to participate in the day-to-day management of the property or properties. Unlike share investors, tenant-in-common investors did not become limited partners or members in the entity that controlled the fund.

The Colton Entities issued a separate private placement memorandum to solicit investors in each fund. They first solicited share investors for a fund and then later solicited tenant-in-common investors for specific properties the fund purchased. Share investors executed a subscription agreement and either an operating agreement or a limited partnership agreement that defined the interests they purchased and the Colton Entities’ rights and obligations. Tenant-in-common investors executed a subscription

agreement, tenant-in-common agreement, and property management agreement to define their interests in the property they purchased and the Colton Entities' rights and obligations regarding the property.

At issue in this case are three funds the Colton Entities created (the Discovery Fund, LLC; the Freedom Fund, LLC; and the Victory Fund, LLC) and four tenant-in-common properties in which the Colton Entities offered interests (the Williams Center, Colton Corporate Center, Union Bank Square, and Town & Country Partners properties). The Colton Entities solicited investors for each of these funds and properties at different times between 1997 and 2003. The Williams Center and Colton Corporate Center properties are part of the Freedom Fund and the tenant-in-common investors in those properties hold title along with the Freedom Fund. The parties do not identify any particular fund associated with the Union Bank Square and Town & Country Partners properties.

One group of Plaintiffs invested only as share investors in the Discovery, Freedom, or Victory Funds. A second group of Plaintiffs invested only as tenant-in-common investors in the Williams Center, Colton Corporate Center, Union Bank Square, or Town & Country Partners properties. A final group of Plaintiffs

invested as both share investors and tenant-in-common investors in the funds and properties the Colton Entities offered. Every Plaintiff made more than one investment.⁴

Plaintiffs filed this action in May 2011, alleging a wide variety of claims against Defendants based on their conduct in soliciting investors and managing the properties held by the funds. Plaintiffs alleged the following claims: (1) financial elder abuse under California law; (2) financial elder abuse under Utah law; (3) fraud; (4) breach of fiduciary duty; (5) unjust enrichment; (6) breach of contract; (7) breach of the implied covenant of good faith and fair dealing; (8) unfair business practices;

⁴ The following table summarizes the investments Plaintiffs made. The complaint failed to identify a specific investment that either plaintiffs Sally Davis or Ezekiel Dumke made. The complaint, however, described Dumke as the manager of Sabio Investments.

Plaintiffs	Share Investments	Tenant-in-Common Investments
Wallace B. & Patricia L. Brown	Discovery Fund Freedom Fund	N/A
Andrew B. & Mary T. Christensen	Discovery Fund	Williams Center
Michael G. Davis Properties	Victory Fund	Williams Center Williams Center Partners Town & Country Partners
Robert H. Davis Properties	Freedom Fund Victory Fund	Colton Corporate Center
DeRose Living Trust	N/A	Williams Center Union Bank Square
Sabio Investments	Discovery Fund Freedom Fund	N/A
Infelise Trust	N/A	Williams Center Union Bank Square
Quast Trust	N/A	Williams Center Union Bank Square
John S. Young	Discovery Fund Freedom Fund	N/A

(9) negligence; (10) failure to make financial information available in violation of Corporations Code section 17106; (11) accounting; and (12) declaratory relief.

Defendants filed two separate motions to compel arbitration. The first motion sought to compel Plaintiffs who invested in the Freedom Fund as tenant-in-common investors to arbitrate their claims relating to the Williams Center and Colton Corporate Center properties. The second motion sought to compel Plaintiffs who invested in any of the three funds as share investors to arbitrate their claims relating to those funds. Neither of the motions addressed the claims by Plaintiffs who invested in the Union Bank Square and Town & Country Partners properties as tenant-in-common investors.

Plaintiffs opposed both motions. They argued the motion against the Freedom Fund tenant-in-common investors should be denied because none of those Plaintiffs agreed to arbitrate their claims. Plaintiffs also argued the court should deny both motions under section 1281.2(c) because Defendants are parties to pending litigation with some investors who did not agree to arbitration, which created the possibility of conflicting rulings on common factual or legal issues. Plaintiffs did not argue the arbitration agreements were unenforceable on any ground other than section 1281.2(c).

The trial court denied both motions. It denied the motion against the Freedom Fund tenant-in-common investors because it found none of those Plaintiffs agreed to arbitrate their claims. The court denied the motion against the share investors based on section 1281.2(c) because it found enforcement of those arbitration agreements would result in some Plaintiffs litigating their claims in court while others arbitrated their claims. The court explained, “[t]he splitting of claims is what Section 1281.2 is designed to avoid” and “the splitting of these Plaintiffs and their claims would be inappropriate,

[and] would result in inconsistent rulings, incomplete remedies and an expenditure of excessive financial resources, among other concerns.” Defendants timely appealed.⁵

II

DISCUSSION

A. *The Freedom Fund Tenant-in-Common Investors Did Not Agree to Arbitration*

Although none of the agreements the Freedom Fund tenant-in-common investors signed included an arbitration provision, Defendants nonetheless argue those Plaintiffs agreed to arbitrate their claims because the agreements they signed *incorporated other agreements that included arbitration provisions*. Defendants point to the following language in paragraph 3(g) of the subscription agreement the Freedom Fund tenant-in-common investors signed: “I (and/or my Professional Advisor) have read and am familiar with the Offering Memorandum, TIC Addendum and all Exhibits, this Subscription Agreement and other related documents.” Because the Freedom Fund’s operating agreement was an exhibit to the offering memorandum, Defendants contend this language incorporates the operating agreement and its arbitration provision into the subscription agreement. Neither paragraph 3(g)’s language nor the law regarding incorporation by reference supports Defendants’ argument.

“[A]n agreement need not *expressly* provide for arbitration, but may do so in a secondary document which is incorporated by reference” (*Chan v. Drexel Burnham Lambert, Inc.* (1986) 178 Cal.App.3d 632, 639, original italics (*Chan*)). “““But

⁵ In March 2011, a different group of nearly 250 investors filed a separate action alleging similar claims regarding Defendants’ conduct in soliciting investors and managing the properties held in the investment funds. The trial court deemed these two actions related and heard Defendants’ motions to compel arbitration in both actions at the same time. The court denied Defendants’ motions in the related action based on section 1281.2(c). We reversed that ruling and remanded the matter for further proceedings in a separate unpublished opinion. (See *Acquire II, Ltd. v. Colton Real Estate Group* (Feb. 11, 2013, G046241) (*Acquire*)).

each case must turn on its facts. [Citation.] For the terms of another document to be incorporated into the document executed by the parties the reference must be clear and unequivocal, the reference must be called to the attention of the other party and he must consent thereto, and the terms of the incorporated document must be known or easily available to the contracting parties.” [Citations.]” (*Id.* at p. 641, italics omitted; see also *Troyk v. Farmers Group, Inc.* (2009) 171 Cal.App.4th 1305, 1331; *Baker v. Osborne Development Corp.* (2008) 159 Cal.App.4th 884, 895.)

In *Chan*, the defendant was a securities brokerage firm that employed the plaintiff as a stockbroker. During her employment, the plaintiff signed a uniform application to register with the National Association of Securities Dealers, the American Stock Exchange, and the New York Stock Exchange (NYSE). The application stated the plaintiff ““agree[d] to abide by the Statute(s), Constitution(s), Rule(s) and By-Laws . . . of the agency jurisdiction or organization with or to which [she submitted the application].”” (*Chan, supra*, 178 Cal.App.3d at p. 636.) The NYSE’s rules required registered stockbrokers to arbitrate any controversy arising out of their employment with a NYSE member. (*Ibid.*) When the plaintiff later sued for wrongful termination, the defendant moved to compel arbitration based on the NYSE’s arbitration rule. The trial court denied the motion, rejecting the defendant’s argument the application the plaintiff signed incorporated the NYSE’s arbitration rule. (*Id.* at pp. 636-637.)

The Court of Appeal affirmed, explaining ““the right to select a judicial forum, vis-a-vis arbitration, is a ““substantial right,”” not lightly to be deemed waived. [Citations.]’ [Citation.]” (*Chan, supra*, 178 Cal.App.3d at p. 643.) The *Chan* court found the vague reference to ““the Statute(s), Constitution(s), Rule(s) and By-Laws”” of any organization to which the application was submitted did not incorporate the NYSE’s arbitration rule into the application because the reference ““failed to *clearly* and *unequivocally* refer to [the NYSE’s rules]”” and nowhere mentioned arbitration. (*Id.* at p. 643, original italics.) In short, the application did not incorporate additional terms

because it failed to direct the plaintiff to a specific document that included other provisions. (*Id.* at pp. 643-644.)

Here, paragraph 3(g) of the subscription agreement likewise failed to incorporate the Freedom Fund operating agreement and its arbitration provision. As in *Chan*, paragraph 3(g) vaguely refers to a variety of other documents, but it does not specifically refer to the operating agreement or mention arbitration. Moreover, paragraph 3(g) does not purport to bind the Freedom Fund tenant-in-common investors to the operating agreement or any other document. In *Chan*, the language the defendant relied upon stated the plaintiff “agree[d] to abide by the Statute(s), Constitution(s), Rule(s) and By-Laws” of the various organizations. (*Chan, supra*, 178 Cal.App.3d at p. 636.) Here, paragraph 3(g) merely states the Freedom Fund tenant-in-common investors “have read and [are] familiar with the Offering Memorandum, TIC Addendum and all Exhibits, this Subscription Agreement and other related documents.” Nothing in this language states the Freedom Fund tenant-in-common investors agreed to be bound by any provision in those documents.

The subscription agreement employed different language when it incorporated and bound the Freedom Fund tenant-in-common investors to other documents. Specifically, paragraph 2 of the subscription agreement states, “The undersigned hereby specifically accepts and adopts each and every provision of the Tenant in Common Agreement and all related property documentation submitted to the TIC Investor for execution.” This provision does not refer to the offering memorandum, its exhibits, or the operating agreement, and therefore the subscription agreement does not incorporate the operating agreement’s arbitration provision.

Citing *Shaw v. Regents of University of California* (1997) 58 Cal.App.4th 44, Defendants argue “[t]he contract need not recite that it ‘incorporates’ another document, so long as it ‘guide[s] the reader to the incorporated document.’” (*Id.* at p. 54.) As explained above, however, the subscription agreement failed to guide the

Freedom Fund tenant-in-common investors to the operating agreement and its arbitration provision, and the subscription agreement did not state those Plaintiffs agreed to anything in the operating agreement. In *Shaw*, the document the parties signed did not state it ““incorporated”” the University Policy Regarding Patents, but the document nonetheless expressly acknowledged the plaintiff was ““not waiving any rights to a percentage or royalty payments received by the University, *as set forth in [the] University Policy Regarding Patents[.]*”” (*Ibid.*, original italics.) This clear and unequivocal reference to the incorporated document readily distinguishes *Shaw*.

“Arbitration exists as a matter of contract, thus a party cannot be compelled into arbitration without agreeing to it in the first place.” (*Gilbert Street Developers, LLC v. La Quinta Homes, LLC* (2009) 174 Cal.App.4th 1185, 1191.) The Freedom Fund tenant-in-common investors never agreed to arbitration and the agreements they signed do not support Defendants’ incorporation by reference argument. Accordingly, we affirm the trial court’s ruling denying Defendants’ motion to compel these Plaintiffs to arbitrate their claims.

B. *The Record Does Not Support Denying Arbitration Based on Pending Litigation with Third Parties Who Did Not Agree to Arbitration*

1. *Governing Legal Principles Regarding Motions to Compel Arbitration*

California law reflects a strong public policy in favor of arbitration as a relatively quick and inexpensive method for resolving disputes. (*Lewis v. Fletcher Jones Motor Cars, Inc.* (2012) 205 Cal.App.4th 436, 443.) To further that policy, section 1281.2 requires a trial court to enforce a written arbitration agreement unless one of three limited exceptions applies. (*Laswell v. AG Seal Beach, LLC* (2010) 189 Cal.App.4th 1399, 1404-1405 (*Laswell*)). Those statutory exceptions arise when (1) a party waives the right to arbitration; (2) grounds exist for revoking the arbitration agreement; and (3) pending litigation with a third party creates the possibility for conflicting rulings on common factual or legal issues. (§ 1281.2, subs. (a)–(c).)

The third party litigation exception applies when (1) “[a] party to the arbitration agreement is also a party to a pending court action or special proceeding with a third party”; (2) the third party action “aris[es] 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.” (§ 1281.2(c).) If all three of these conditions are satisfied, then section 1281.2(c) grants the trial court discretion to either deny or stay arbitration despite an agreement to arbitrate the dispute. (*Laswell, supra*, 189 Cal.App.4th at p. 1405.) Specifically, section 1281.2(c) identifies four options from which the court may choose: (1) “refuse to enforce the arbitration agreement and . . . order intervention or joinder of all parties in a single action or special proceeding”; (2) “order intervention or joinder as to all or only certain issues”; (3) “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”; and (4) “stay arbitration pending the outcome of the court action or special proceeding.” (§ 1281.2(c).)

A trial court has no discretion to deny or stay arbitration unless all three of section 1281.2(c)’s conditions are satisfied. (*Molecular Analytical Systems v. CIPHERGEN Biosystems, Inc.* (2010) 186 Cal.App.4th 696, 709 (*Molecular Analytical*) [“The court’s discretion under section 1281.2, subdivision (c) does not come into play until it is ascertained that the subdivision applies . . .”]; see also *Laswell, supra*, 189 Cal.App.4th at p. 1405; *Rowe v. Exline* (2007) 153 Cal.App.4th 1276, 1288, fn. 6 (*Rowe*).)

2. We Infer All Necessary Findings Supported by the Record Because Defendants Failed to Request a Statement of Decision

Upon a party’s timely and proper request, section 632 requires a trial court to issue a statement of decision following “the trial of a question of fact by the court.” The statement must explain “the factual and legal basis for [the court’s] decision as to each of the principal controverted issues at trial.” (§ 632.) California’s statutory scheme regarding contractual arbitration also requires a statement of decision for any ruling

denying a motion to compel arbitration if a party requests one. (§ 1291 [“A statement of decision shall be made by the court, if requested pursuant to [s]ection 632, whenever an order or judgment . . . is made that is appealable under this title”]; *Metis Development LLC v. Bohacek* (2011) 200 Cal.App.4th 679, 687 (*Metis*) [“the Legislature intended to require the trial court to issue a statement of decision, upon proper request under section 632, when denying a petition to compel arbitration”].) No statement of decision is required if the parties fail to request one. (*Agri-Systems, Inc. v. Foster Poultry Farms* (2008) 168 Cal.App.4th 1128, 1134 (*Agri-Systems*); see also *Stermer v. Modiano Constr. Co.* (1975) 44 Cal.App.3d 264, 271.)

A party’s failure to request a statement of decision when one is available has two consequences. First, the party waives any objection to the trial court’s failure to make all findings necessary to support its decision. Second, the appellate court applies the doctrine of implied findings and presumes the trial court made all necessary findings supported by substantial evidence. (*Agri-Systems, supra*, 168 Cal.App.4th at p. 1135.) This doctrine “is a natural and logical corollary to three fundamental principles of appellate review: (1) a judgment is presumed correct; (2) all intendments and presumptions are indulged in favor of correctness; and (3) the appellant bears the burden of providing an adequate record affirmatively proving error.” (*Fladeboe v. American Isuzu Motors, Inc.* (2007) 150 Cal.App.4th 42, 58.)

Here, section 1291 permitted Defendants to request a statement of decision on the principal controverted issue: Whether Plaintiffs met section 1281.2(c)’s three conditions to vest the trial court with discretion to deny Defendants’ motion. Defendants failed to request a statement of decision and therefore waived on appeal any objection based on the trial court’s failure to make all findings necessary to support the court’s ruling under section 1281.2(c). Accordingly, the only question before us is whether the record supports the trial court’s implied finding each of section 1281.2(c)’s conditions

were satisfied. (*Fair v. Bakhtiari* (2011) 195 Cal.App.4th 1135, 1148; *Shaw v. County of Santa Cruz* (2008) 170 Cal.App.4th 229, 267.)

Defendants contend the doctrine of implied findings does not apply because a statement of decision generally is not required for a law and motion matter, such as a motion to compel arbitration. Defendants fail to recognize section 1291 expressly authorized a statement of decision, which explains why none of the cases Defendants cite involves section 1291 or any comparable statute. Indeed, the *Metis* decision rejected Defendants' premise a motion to compel arbitration is an ordinary law and motion matter: "[A] petition [to compel arbitration] is heard *in the manner* of a motion, with factual issues determined upon declarations or, if necessary, live testimony. [Citations.] But a petition to compel arbitration is ""in essence a suit in equity to compel specific performance of a contract."" [Citation.] Unlike most motions, it provides a final determination of certain factual issues . . . and results in an appealable order. Moreover, in ruling on the petition when factual matters are in dispute, the court must weigh credibility and the strength of competing evidence. [Citation.] As such, a hearing on a petition to compel arbitration has attributes of a trial that suggest the need for a statement of decision to enable meaningful appellate review." (*Metis, supra*, 200 Cal.App.4th at p. 688, original italics.)

Although Plaintiffs point out Defendants' failure to request a statement of decision, they nonetheless argue we should review the trial court's ruling under the abuse of discretion standard. But the issue is not whether the trial court abused the discretion granted by section 1281.2(c), but whether the trial court erred in deciding section 1281.2(c) applied. In other words, the issue is whether the trial court erred by impliedly finding each of section 1281.2(c)'s conditions were satisfied.⁶

⁶ We note Defendants alternatively assert the trial court abused its discretion under section 1281.2(c). Given our conclusion the trial court erred in finding

When section 1281.2(c) applies, “the trial court’s discretionary decision as to whether to stay or deny arbitration is subject to review for abuse.” (*Laswell, supra*, 189 Cal.App.4th at p. 1406; *Birl v. Heritage Care, LLC* (2009) 172 Cal.App.4th 1313, 1318; *Rowe, supra*, 153 Cal.App.4th at p. 1283.) The trial court’s decision whether section 1281.2(c) applies, however, is reviewed under either the substantial evidence standard or de novo standard. If the court based its decision on a legal determination, then we adopt the de novo standard. (*Laswell*, at p. 1406 [whether a party constitutes a third party under section 1281.2(c) is a legal question subject to de novo review]; *Molecular Analytical, supra*, 186 Cal.App.4th at pp. 708-709.) If the court based its decision on a factual determination, then we adopt the substantial evidence standard of review. (*Laswell*, at p. 1406.) Whether there are conflicting issues arising out of related transactions is a factual determination subject to review under the substantial evidence standard. (*Metis, supra*, 200 Cal.App.4th at p. 691, fn. 7.)

We emphasize the allegations of the parties’ pleadings may constitute substantial evidence sufficient to support a trial court’s finding that section 1281.2(c) applies. (*Abaya v. Spanish Ranch I, L.P.* (2010) 189 Cal.App.4th 1490, 1498-1499 (*Abaya*)).) A party relying on section 1281.2(c) to oppose a motion to compel arbitration does not bear an evidentiary burden to establish a likelihood of success or make any other showing regarding the viability of the claims and issues that create the possibility of conflicting rulings. (*Abaya*, at pp. 1498-1499.) An evidentiary burden is unworkable under section 1281.2(c) because the question presented is whether a “possibility” of conflicting rulings exists (*id.* at p. 1499) and a motion to compel arbitration is typically brought before the parties have conducted discovery. Moreover, section 1281.2(c) prohibits a trial court from considering the merits of a party’s claims when ruling on a

section 1281.2(c) applied on the current record, we need not decide whether the trial court abused its discretion under section 1281.2(c).

motion to compel arbitration. (§ 1281.2(c); *California Correctional Peace Officers Assn. v. State of California* (2006) 142 Cal.App.4th 198, 205, 211.)

Accordingly, the issue before us is whether the allegations of the parties' pleadings or other evidence in the record support an implied finding that Plaintiffs' claims arise out of a series of related transactions and create the possibility of conflicting rulings on common factual and legal issues.⁷ None of the parties dispute Defendants are parties to pending litigation with third parties who did not agree to arbitrate their claims.

3. The Record Does Not Support the Implied Finding Section 1281.2(c)'s Conditions Were Satisfied

Defendants' motion sought to compel three distinct groups of share investors to arbitrate their claims: the Discovery Fund share investors, the Freedom Fund share investors, and the Victory Fund share investors. The trial court denied Defendants' motion in its entirety based on section 1281.2(c) without separately addressing each of the three conditions required for that subdivision to apply. Accordingly, to affirm the trial court's ruling we must find substantial evidence in the record to support the implied finding section 1281.2(c)'s three conditions were satisfied for each of these three groups of share investors.

⁷ Although allegations in a pleading may support a trial court's finding section 1281.2(c)'s conditions are satisfied, a party may not make frivolous or unsupported allegations to defeat a motion to compel arbitration. By making allegations in a pleading and later advocating those allegations to the court, an attorney or unrepresented party "certif[ies]" (1) "The claims, defenses, and other legal contentions therein are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law"; (2) "The allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery"; and (3) "The denials of factual contentions are warranted on the evidence or, if specifically so identified, are reasonably based on a lack of information or belief." (§ 128.7, subd. (b)(2)-(4).) If any of these certifications are false, the attorney or unrepresented party is subject to sanctions. (§ 128.7, subd. (d).)

For example, to affirm the trial court's decision denying Defendants' motion to compel the Discovery Fund share investors to arbitrate their claims, the record must contain substantial evidence to support the findings that (1) Defendants are involved in pending litigation with third parties who did not agree to arbitration (e.g., the Freedom Fund tenant-in-common investors or the tenant-in-common investors who invested in the Town & Country Partners or Union Bank Square properties); (2) the claims of the Discovery Fund share investors and the claims of at least one of these third parties arose out of the same transaction or series of related transactions; and (3) a factual or legal issue common to the claims of the Discovery Fund share investors and at least one of the third parties created the potential for conflicting rulings.

After reviewing the entire record, we are unable to find substantial evidence to support the findings required to deny Defendants' motion as to any of the three groups of share investors based on section 1281.2(c). Although the record shows some parties to the arbitration agreements (i.e., Defendants) also are defending claims brought by third parties who did not agree to arbitration, the record fails to show that (1) the claims of share investor Plaintiffs who agreed to arbitration and the claims of any group of Plaintiffs who did not agree to arbitration arose out of the same transaction or series of related transactions; *and* (2) the claims of those same two groups of Plaintiffs share a common factual or legal issue that creates the possibility of conflicting rulings.

Plaintiffs' claims regarding their decisions to invest with Defendants arose out of separate transactions because each group of Plaintiffs invested in different funds or properties at different times over a six-year period. Defendants offered investment opportunities in each fund and property under separate private placement memoranda months or years apart. Even the share investment and tenant-in-common investment opportunities in the same fund were offered at different times. Each group of Plaintiffs executed separate agreements to define their rights and obligations depending on the fund or property in which they invested.

Plaintiffs' claims regarding Defendants' management of the funds and properties also arose out of separate transactions because Defendants managed different funds and different properties for each group of Plaintiffs. A transaction regarding one property or fund did not affect a separate property held in a separate fund. Separate agreements governed Defendants' management of each fund and each group of properties. Specifically, Defendants managed the properties the funds held for the share investors under separate operating agreements governing each fund and they managed the separate properties each fund owned with the tenant-in-common investors under separate property management agreements.

For similar reasons, the record does not show a common factual or legal issue that would create the possibility of conflicting rulings between those Plaintiffs who agreed to arbitration and those who did not. Defendants' alleged misconduct related to different funds and properties, occurred at different times, and different contracts applied for each group of Plaintiffs.

Plaintiffs argue section 1281.2(c) applies to all of their claims because Defendants engaged in the same pattern of mismanagement as to all funds and properties. Plaintiffs, however, fail to cite any allegations in their complaint or other evidence in the record to show how Defendants' conduct in managing separate properties held in separate funds arose from the same transaction or a series of related transactions, or how Defendants' conduct in managing separate properties and funds created the possibility of conflicting rulings on common factual or legal issues. Because the record shows each fund owned and managed separate properties governed by separate agreements entered into at different times, Plaintiffs' bare conclusion that Defendants engaged in the same pattern of mismanagement with all properties and funds fails to satisfy section 1281.2(c)'s requirements. Plaintiffs must point to specific allegations in their complaint or other evidence in the record showing how separate transactions regarding separate properties and funds amount to a series of related transactions *and* how the

claims regarding those separate transactions present the possibility of conflicting rulings on legal or factual issues common to the claims arising from those separate transactions. (See *Metis, supra*, 200 Cal.App.4th at pp. 691-692 [section 1281.2(c) requires a specific issue common to the arbitrable and nonarbitrable claims].) Plaintiffs cannot defeat Defendants' contractual right to arbitration by simply joining Plaintiffs who agreed to arbitration with Plaintiffs who invested in a separate fund or property and did not agree to arbitration.⁸

Plaintiffs provided a few examples of claims they contend arose out of related transactions and share a common issue creating the possibility of conflicting rulings. None of Plaintiffs' examples, however, shows all three of section 1281.2(c)'s conditions were satisfied for any single group of share investors. At best, Plaintiffs' examples potentially satisfy one or two of section 1281.2(c)'s conditions for a particular group of Plaintiffs. But even when considered together, Plaintiffs' examples fail to show all three of section 1281.2(c)'s conditions were satisfied for any single group of Plaintiffs.

Plaintiffs borrow their first example from the plaintiffs in the related *Acquire* action. Specifically, Plaintiffs cite the *Acquire* plaintiffs' contention the Freedom Fund improperly loaned approximately \$7.2 million to a partnership that owned "Discovery Fund Property [N]umber 4," an entity not subject to arbitration. According to Plaintiffs, Defendants breached the duties they owed the Freedom Fund share investors

⁸ Plaintiffs' brief focuses on Defendants' conduct in managing the funds and separate properties as the basis for satisfying section 1281.2(c)'s conditions, but they did not argue Defendants' conduct in fraudulently inducing Plaintiffs to invest in the funds and properties satisfied section 1281.2(c)'s conditions. Plaintiffs fail to explain how claims arising out of separate investments made by different people, at different times, and relating to separate properties and funds amount to the same transaction or series of related transactions, or how claims arising out of these separate investments in different funds and properties share common factual or legal issues creating the possibility of conflicting rulings.

by making this loan rather than distributing the funds to the investors, and Defendants also breached the duties they owed the Discovery Fund tenant-in-common investors by taking a loan at what Plaintiffs contend was an exorbitant interest rate. Although the claims relating to this loan may arise out of the same transaction, they do not present a common factual or legal issue creating the possibility of conflicting rulings.

Making and taking a loan are opposite sides of the same transaction and each involves different risks and obligations. The Freedom Fund's operating agreement governed Defendants' conduct in making the loan while the Discovery Fund's tenant-in-common agreement and property management agreement governed Defendants' conduct in taking the loan. A ruling Defendants breached their duties to the Freedom Fund share investors by making the loan and a ruling Defendants did not breach their duties to the Discovery Fund tenant-in-common investors by taking the loan (or vice versa) are not conflicting rulings on a common factual or legal issue because different rights and duties are involved on each side of the transaction.

Plaintiffs also borrow their second example from the *Acquire* plaintiffs. Specifically, Plaintiffs rely on the *Acquire* plaintiffs' contention that "parcel number 3" is a single parcel of land that includes two office buildings owned by different funds — one owned by the Victory Fund and one owned by the Freedom Fund — without separately recording these interests on the title. According to Plaintiffs, this parcel shows the Victory and Freedom Funds are "tied at the hip" and have claims arising out of the same transaction or series of related transactions. Plaintiffs, however, identify no factual or legal issue regarding this parcel common to the claims of the Victory Fund and Freedom Fund Plaintiffs that could create conflicting rulings. Indeed, Plaintiffs identify no specific claim relating to this parcel at all.

Plaintiffs' third example involves three Plaintiffs who invested as share investors in one of the three funds and also invested as tenant-in-common investors in one or more individual properties. Plaintiffs contend enforcing the share investors'

arbitration agreements would require these three Plaintiffs to litigate their tenant-in-common investor claims while simultaneously arbitrating their share investor claims. But Plaintiffs identify no specific factual or legal issue common to these Plaintiffs' claims that could create the possibility of conflicting rulings. More importantly, these Plaintiffs are not third parties for section 1281.2(c)'s purposes because they each agreed to arbitrate some of their claims even though they did not agree to arbitrate all of them.

“A trial court does not have discretion to deny arbitration under . . . section [1281.2(c)], absent the presence of a third party” (*Laswell, supra*, 189 Cal.App.4th at p. 1409.) “The term ‘third party’ for purposes of section 1281.2[(c)], must be construed to mean a party that is not bound by the arbitration agreement.” (*RN Solutions, Inc. v. Catholic Healthcare West* (2008) 165 Cal.App.4th 1511, 1519 (*RN Solutions*); *Laswell*, at p. 1407.) “[A] plaintiff’s inclusion of a nonarbitrable cause of action in the complaint is not grounds to deny arbitration under the third party exception. In other words, the presence of a nonarbitrable cause of action is not sufficient by itself to invoke the trial court’s discretion to deny arbitration under . . . section [1281.2(c)]” (*Laswell*, at p. 1409; *RN Solutions*, at p. 1521.)

When the dispute between parties to an arbitration agreement includes both arbitrable and nonarbitrable claims, section 1281.2(c) limits the trial court’s discretion to delaying arbitration, and only if the court first determines that resolving the nonarbitrable claims in court may make arbitration of the arbitrable claims unnecessary. (*RN Solutions, supra*, 165 Cal.App.4th at pp. 1521-1522; see also § 1281.2(c) [“If the court determines that there are other issues between the petitioner and the respondent which are not subject to arbitration and which are the subject of a pending action or special proceeding between the petitioner and the respondent and that a determination of such issues may make the arbitration unnecessary, the court may delay its order to arbitrate until the determination of such other issues or until such earlier time as the court specifies”].) Accordingly, the

fact a Plaintiff who made multiple investments may have to arbitrate his or her claims regarding one investment and litigate his or her claims regarding another investment is not a ground for denying arbitration under section 1281.2(c).

At oral argument, Plaintiffs offered additional examples of common issues they contend satisfied section 1281.2(c)'s requirements. Specifically, Plaintiffs argued a factual issue common to all Plaintiffs' claims arose when Defendants concealed that David Colton had a multimillion dollar fraud judgment for running an investment scheme similar to the one at issue in this case. Plaintiffs also argued the misrepresentations Defendants made to induce them to invest with Defendants presented common factual issues because Defendants made the misrepresentations during essentially identical investment seminars Defendants conducted. Unfortunately for Plaintiffs, they did not argue these purported common issues in their brief and they may not raise this point for the first time at oral argument.⁹ (*Palp, Inc. v. Williamsburg National Ins. Co.* (2011) 200 Cal.App.4th 282, 291, fn. 2 [“We do not consider arguments that are raised for the first time at oral argument”]; *Rosen v. St. Joseph Hospital of Orange County* (2011) 193 Cal.App.4th 453, 464, fn. 4.) Moreover, whether Defendants made the same representations to, or concealed the same information from, all Plaintiffs is not a common factual issue that could lead to conflicting rulings if Defendants solicited Plaintiffs at different times and had separate transactions with different Plaintiffs. Indeed, a finding Defendants made a particular misrepresentation to one Plaintiff, and a finding Defendants

⁹ The introduction to Plaintiffs' brief refers to the prior judgment against David Colton and suggests he used the fraudulent scheme at issue in that case as the framework for the investments Defendants sold to Plaintiffs. Plaintiffs' brief, however, does not argue Defendants' failure to disclose the prior judgment presents a common issue that satisfies section 1281.2(c)'s requirements. Indeed, the argument section of Plaintiffs' brief fails to refer to the prior judgment at all. Plaintiffs' brief also includes no reference to any investment seminars where Defendants' allegedly made the same misrepresentations to all Plaintiffs.

did not make the same misrepresentation to another Plaintiff at a later time, do not constitute conflicting rulings on a common factual issue because the transactions occurred at different times. Whether Defendants had a duty to disclose certain information to all Plaintiffs could be a common legal issue, but Plaintiffs did not argue that in their briefs.

Plaintiffs also repeatedly emphasize that compelling the share investors to arbitrate their claims while allowing the tenant-in-common investors to litigate their claims would result in “substantial duplication of effort” and “logistical problems” because Plaintiffs would have to present much of the same evidence and call many of the same witnesses in both forums. Plaintiffs also emphasize (1) the vast majority of their money is invested in tenant-in-common investments that are not subject to arbitration agreements; and (2) the majority of Plaintiffs are entitled to trial preference because they are over 70 years old. But these considerations become relevant only if section 1281.2(c)’s conditions are satisfied.

A trial court must first determine whether section 1281.2(c) applies. Only then may the court consider judicial economy and other similar factors in deciding how to exercise the discretion section 1281.2(c) confers — for example, whether to deny arbitration and require all parties to litigate their dispute, whether to stay arbitration while the litigation proceeds, or whether to stay the litigation while the arbitration proceeds. (See *Cronus Investments, Inc. v. Concierge Services* (2005) 35 Cal.4th 376, 393; *Doan v. State Farm General Ins. Co.* (2011) 195 Cal.App.4th 1082, 1100-1101.) But a trial court must decide whether section 1281.2(c) applies based only on the three conditions identified in that subdivision. (See *Laswell, supra*, 189 Cal.App.4th at p. 1405; *Molecular Analytical, supra*, 186 Cal.App.4th at p. 709; *Rowe, supra*, 153 Cal.App.4th at p. 1288, fn. 6.) Section 1281.2(c)’s primary purpose is to avoid conflicting rulings, not further judicial economy. (See *Whaley v. Sony Computer Entertainment America, Inc.* (2004) 121 Cal.App.4th 479, 488 [“the statute was intended primarily to prevent

conflicting rulings resulting from arbitration proceedings and other related litigation arising out of the same transaction”].)

Finally, based on *Abaya*, Plaintiffs argue claimants who join together to sue the same defendants on the same claims satisfy section 1281.2(c)’s conditions when some of the claimants agreed to arbitration and others did not. *Abaya* is distinguishable and provides no support for Plaintiffs’ position the trial court properly denied Defendants’ motion against the share investors.

In *Abaya*, approximately 120 mobilehome park residents sued the park’s owners, alleging a variety of claims based on the owners’ failure to maintain the park’s common facilities. Many of the plaintiffs’ leases included an arbitration provision, but approximately 20 to 30 did not. Based on section 1281.2(c), the trial court denied the owners’ motion to compel the plaintiffs with arbitration agreements to arbitrate their claims. (*Abaya, supra*, 189 Cal.App.4th at pp. 1493-1495.) The Court of Appeal affirmed the trial court’s decision that section 1281.2(c)’s conditions were satisfied because whether the park owners adequately maintained the common facilities was an issue common to each plaintiff’s claim regardless whether his or her lease included an arbitration provision. Resolving this common issue in different forums could lead to conflicting rulings. (*Abaya*, at p. 1498.)

Abaya is distinguishable because the plaintiffs in *Abaya* lived in the same mobilehome park and complained about the owners’ management of the same common facilities. Here, Plaintiffs are investors in three separate investment funds and four separate properties who complain about Defendants’ conduct in inducing separate investments and managing separate properties. *Abaya* would be analogous if this case involved a single investment fund because Plaintiffs would be asserting claims relating to their investment in the same fund and Defendants’ management of the same properties.

Although not raised by Plaintiffs, *Abaya* nonetheless points to a basis on which the trial court potentially could deny at least a portion of Defendants’ motion

against the share investors under section 1281.2(c). Specifically, the trial court may base a denial on the possibility of conflicting rulings regarding claims share investors and tenant-in-common investors in the same fund assert against Defendants for their management of the same piece of property when the share investors agreed to arbitration, but the tenant-in-common investors did not.

As explained above, each of the three funds at issue had two types of investors: share investors and tenant-in-common investors. The share investors became partners or members in the entity that took title to the properties the fund purchased and managed, but did not own an interest in any specific property. The tenant-in-common investors purchased an ownership interest in one or more specific properties the fund owned and held a tenant-in-common ownership interest in the property or properties with the fund. The tenant-in-common investors were not partners or members in the entity that is the fund.

If the share investors in a fund assert a claim that Defendants engaged in misconduct relating to their management of a specific property, and the tenant-in-common investors in the same fund assert that Defendants engaged in misconduct relating to their management of the same property, a common factual or legal issue creating the potential for conflicting rulings exists if the share investors in that fund agreed to arbitration and the tenant-in-common investors in the same fund did not. This poses a different conflict from the examples Plaintiffs provided because the Plaintiffs in this situation are investors in the same fund and the tenant-in-common investor did not agree to arbitrate any of his or her claims. An example that would fulfill these criteria is a Freedom Fund share investor and a Freedom Fund tenant-in-common investor, provided both investors assert Defendants mismanaged the same property and the tenant-in-common investor did not sign an arbitration agreement with Defendants regarding another fund or property.

Plaintiffs do not identify a specific share investor and tenant-in-common investor who would satisfy these criteria. Plaintiffs' operative pleading at the time the trial court ruled on Defendants' motion did not identify any specific property Defendants allegedly mismanaged and the few examples discussed above do not satisfy the foregoing criteria. As a result, the record lacks substantial evidence to support the implied findings necessary to uphold the trial court's ruling based on a potential conflict between claims held by share investors and tenant-in-common investors in the same fund regarding the same property.¹⁰

Based on the foregoing, we must reverse the trial court's ruling denying Defendants' motion to compel the share investors to arbitrate their claims. Both Plaintiffs and the trial court treated all Plaintiffs as one large group and failed to separately examine each of section 1281.2(c)'s conditions for each group of Plaintiffs. Although the claims of each group of Plaintiffs may generally relate to one another because they all relate to investment funds formed and operated by Defendants, and although it may be more efficient to decide all these claims in one forum, neither of those considerations satisfy section 1281.2(c)'s conditions. California law favors arbitration as a dispute resolution method. Consequently, a trial court may deny a party's contractual right to arbitration only when all of section 1281.2(c)'s conditions are satisfied. California courts have no inherent authority to deny arbitration simply because it would be more efficient to litigate the claims in court.

At oral argument, the parties agreed the appropriate remedy for the trial court's erroneous ruling was to remand for further consideration under section 1281.2(c). Accordingly, we remand this matter for the trial court to separately consider each group of share investors to determine whether their claims satisfy all three of

¹⁰ We do not suggest the foregoing are the only possible issues that could satisfy section 1281.2(c)'s requirements. Rather, we merely point out these issues as possibilities based on the issues Plaintiffs argued in their brief.

section 1281.2(c)'s conditions. (*Metis, supra*, 200 Cal.App.4th at pp. 693-694 [remanding to further consider whether section 1281.2(c)'s conditions were satisfied when appellate record failed to identify common issues the trial court relied upon to exercise its discretion under section 1281.2(c)].)

In opposing Defendants' motion, Plaintiffs must provide the trial court with sufficient information regarding their claims to support a finding the claims of Plaintiffs who agreed to arbitration and the claims of Plaintiffs who did not agree to arbitration share a common factual or legal issue that could result in conflicting rulings. As explained above, allegations regarding Defendants' misconduct may satisfy this burden because Plaintiffs have no evidentiary burden to establish their claims at this stage of the proceedings.¹¹ (*Abaya, supra*, 189 Cal.App.4th at pp. 1498-1499.)

If the trial court finds section 1281.2(c)'s conditions are satisfied for any group of share investors, then it must decide how best to exercise the discretion that subdivision provides. The trial court is not limited to merely denying arbitration. The court also may deny arbitration only for certain claims or parties, stay some or all of the claims subject to arbitration until the litigation is completed, or stay some or all of the claims subject to litigation until the arbitration is completed. "What the trial court chooses to do in this situation is a matter of its discretion, guided largely by the extent to which the possibility of inconsistent rulings may be avoided." (*Metis, supra*, 200 Cal.App.4th at pp. 692-693.) We express no opinion on whether section 1281.2(c)'s conditions may be satisfied for any group of share investors or how the trial court should exercise its discretion if it finds section 1281.2(c)'s conditions have been met.

¹¹ We leave to the trial court's discretion whether the parties should file supplemental briefs addressing the issues raised in this opinion or allow Defendants to file a new motion.

III

DISPOSITION

We affirm the order denying Defendants' motion to compel the Freedom Fund tenant-in-common investors to arbitrate their claims. We reverse the order denying Defendants' motion to compel the share investors to arbitrate their claims and remand for further proceedings consistent with this opinion. In the interest of justice, all parties shall bear their own costs on appeal.

ARONSON, ACTING P. J.

WE CONCUR:

FYBEL, J.

IKOLA, J.