FROG CREEK v. VANCE BROWN, INC.

Court of Appeal of California, First Appellate District, Division Five
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FROG CREEK PARTNERS, LLC, Plaintiff and Respondent, v. VANCE BROWN, INC., Defendant and Appellant.

Prior History: San Mateo County Super. Ct. No. CIV 445004.

Core Terms

arbitration, trial court, arbitration clause, inducement, contractual, arbitration agreement, motion to compel arbitration, binding, existence of a contract, federal court, inception

Judges: REARDON, J. [*]SIMONS, Acting P.J., GEMELLO, J. concurred.

Opinion by: REARDON

Opinion

Appellant Vance Brown, Inc., appeals from an order of the trial court, denying appellant's motion to compel arbitration of a lawsuit brought by respondent ***Frog Creek*** Partners, LLC. We affirm.

I. FACTS AND PROCEDURAL HISTORY

This appeal arises out of the construction of a $ 13 million dollar residential complex on Bridle Lane in Woodside. This complex is intended to be a home for Jeffrey Drazan, the managing director of a venture capital firm, Sierra Ventures. Drazan formed his own limited liability company, respondent ***Frog Creek*** Partners, LLC (***Frog Creek***) to manage the **[*2]** construction project.

Frog Creek selected appellant Vance Brown, Inc. (Brown), to build the project. Brown began work on the project on September 18, 2002. [1] On September 20th, Brown presented ***Frog Creek*** with a first draft of a contract. This draft included a dispute resolution provision requiring mediation of all disputes followed, if necessary, by arbitration of all disputes involving $ 50,000 or less. On September 24th, counsel for ***Frog Creek*** responded with a five-page letter suggesting various changes to the contract, including elimination of the $ 50,000 cap on disputes subject to arbitration. The suggested change to the dispute resolution provision was made in the final draft of the contract.

Thereafter, the parties signed separate copies of the **[*3]** final draft contract, as was permitted by the contract. However, the copy signed by ***Frog Creek*** contained several handwritten amendments to the contract language. The copy signed by Brown did not contain these amendments. The parties presented no single contract containing signatures of representatives of both parties, nor have they presented separate *but identical* signed versions of the contract. They appear to agree that no such documents exist. Additionally, there is no dispute that the handwritten changes on the ***Frog Creek*** copy of the contract were unrelated to the dispute resolution provi-

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[*] Judge of the Superior Court of Alameda County, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

[1] The work involved numerous subcontractors and suppliers; one of the subcontractors was an out of state firm, and many supplies for the project were obtained from out of state. The parties do not dispute that the project was one involving interstate commerce.

sion. [2]

[*4] Per the document, the guaranteed maximum cost (GMC) was $ 10,536,901, ″subject to approved Change Orders.″ The document also indicates that the GMC ″includes an allowance of $ 1,051,086 for landscaping and irrigation . . . .″ However, on the ***Frog Creek*** copy, there is a handwritten interlineation of the figure $ 1,300,000. Additionally, requirements regarding providing electrical power to a stable and a well were added in handwriting. Finally, there were minor handwritten changes regarding the timing of and communication between the parties regarding weekly project team meetings.

In his declaration submitted in opposition to Brown's motion, Drazen states that he discussed these changes with Brown and indicated that he was not willing to enter into an agreement without them. Drazen submitted as an exhibit to his declaration an e-mail from Brown, dated December 4, 2002 and reading: ″Can we pick up a copy of the signed FC construction agreement with your notes? I want to follow up on the clean-up.″ Drazen also states that an addition of more than $ 200,000 to the landscaping costs was significant, because it represented one-third of the contractor's fee to be paid to Brown. Indeed a **[*5]** further e-mail from Brown, dated April 5, 2004, reads, in part: ″We have a dispute about the $ 1,300,000 number that you unilaterally inserted in one page of the Construction Agreement that showed a Landscape Allowance of $ 1,051,086 in numerous other places.″

In 2005, ***Frog Creek*** brought this lawsuit against Brown, asserting causes of action arising out of the construction project, including breach of contract and conversion. The merits of those claims are not now before us on this appeal, which arises solely from the trial court's denial of Brown's motion to compel arbitration. However, we note, in aid of alleging its contractual and other claims, ***Frog Creek*** attached a copy of its version of the written agreement, which, like Brown's version, contains the arbitration provision in issue here.

Frog Creek then sought to resolve the litigation by invoking mediation; however, mediation was unsuccessful. Brown then filed a motion to compel arbitration, which was denied by the trial court. [3] Brown, thereafter, requested a statement of decision; ***Frog Creek*** opposed this request as untimely. The court denied the request without explanation, and this appeal followed.

[*6] II. DISCUSSION

″[W]hen a petition to compel arbitration is filed and accompanied by prima facie evidence of a written agreement to arbitrate the controversy, the court itself must determine whether the agreement exists and, if any defense to its enforcement is raised, whether it is enforceable. Because the existence of the agreement is a statutory prerequisite to granting the petition, the petitioner bears the burden of proving its existence by a preponderance of the evidence.″ (*Rosenthal v. Great Western Fin. Securities Corp.* (1996) 14 Cal.4th 394, 413 (*Rosenthal*).) Brown, as the petitioner, was required to establish the existence of the contract. ***Frog Creek*** contends Brown failed to establish that Brown's version of the agreement was, indeed, a contract, and, more specifically, that whether it was a contract was a question for the trial court and not the arbitrator. We agree as to both.

We turn first to whether the question of the existence of a contract at all is one for the court or the arbitrator. Because the matter before us is one involving interstate commerce, it is governed by the United States Arbitration Act, or the USAA (*9 U.S.C. §§ 1* **[*7]** -16), and cases interpreting that act. (*Rosenthal, supra*, 14 Cal.4th at p. 405.) Section 4 of the USAA provides, in part: ″The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in

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[2] As to arbitration, the dispute resolution provision states, in pertinent part: ″**25.4** If the dispute is not resolved within thirty (30) days after the conclusion of the mediation then the dispute shall be resolved in an arbitration to be conducted in accordance with the terms of **Paragraph 25.5**, below. [P] **25.5** If the dispute is to be the subject of an arbitration, either party may, at its own option, initiate the arbitration by delivering written notice to the other party to the dispute. All parties to the dispute shall attend and participate in, and shall be bound by the results of, the arbitration proceeding. The arbitration shall be conducted in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association then in effect, as supplemented by the terms of this paragraph. During the pendency of any arbitration proceeding, the parties shall continue to perform all obligations under this Agreement. All arbitration proceedings shall be held in San Francisco, California, before a single neutral arbitrator having at least 10 years of relevant experience in design and construction matters. The arbitrator will be selected from a list of potential arbitrators provided by the American Arbitration Association. Each party shall make all of its project documents available for the other party to inspect and copy at least ten (10) days in advance of the arbitration. No other discovery will be permitted in connection with the arbitration. The arbitrator's award shall be in writing, and shall contain conclusion[s] of law and finding[s] of fact. Judgment upon the award may be entered in any court having jurisdiction. [P] **25.6** This Agreement shall be construed in accordance with and governed by the laws of the State of California.″

[3] To this motion, Brown attached only two pages of the written agreement-those specifically addressing dispute resolution. Ultimately, Brown produced its version of the entire contract, which is signed only by Brown and contains none of Frog Creek's interlineations.

accordance with the terms of the agreement. . . . If the making of the arbitration agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof." The seminal case on this point is *Prima Paint v. Flood & Conklin* (1967) 388 U.S. 395, 403-404, 18 L. Ed. 2d 1270 (*Prima Paint*), in which the court wrote: "Under § 4, with respect to a matter within the jurisdiction of the federal courts save for the existence of an arbitration clause, the federal court is instructed to order arbitration to proceed once it is satisfied that 'the making of the agreement for arbitration or the failure to comply [with the arbitration agreement] is not in issue.' Accordingly, if the claim is fraud in the inducement of **[*8]** the arbitration clause itself-an issue which goes to the 'making' of the agreement to arbitrate-the federal court may proceed to adjudicate it. But the statutory language does not permit the federal court to consider claims of fraud in the inducement of the contract generally." (Brackets in original, fns. omitted.)

Our own Supreme Court has further elucidated this principle: "To consider [a] *Prima Paint* argument, we must separate out the two fraud theories upon which plaintiffs have relied to avoid enforcement of the arbitration agreements: fraud in the *execution* of the client agreements, and fraud '*permeating*' the agreements. [P] California law distinguishes between fraud in the 'execution' or 'inception' of a contract and fraud in the 'inducement' of a contract. In brief, in the former case '"the fraud goes to the inception or execution of the agreement, so that the promisor is deceived as to the nature of his act, and actually does not know what he is signing, or does not intend to enter into a contract at all, mutual assent is lacking, and [the contract] is *void*. In such a case it may be disregarded without the necessity of rescission."' [Citation.] Fraud **[*9]** in the inducement, by contrast, occurs when '"the promisor knows what he is signing but his consent is *induced* by fraud, mutual assent is present and a contract is formed, which, by reason of the fraud, is *voidable*. In order to escape from its obligations the aggrieved party must *rescind* . . . ."' [Citation.] [P] . . . [P] . . . [W]e conclude claims of fraud in the execution of the entire agreement are not arbitrable under either state or federal law. If the entire contract is void *ab initio* because of fraud, the parties have not agreed to arbitrate any controversy; under that circumstance, *Prima Paint* does not require a court to order arbitration. [Citations.] [P] The central rationale of the high court's decision in *Prima Paint* was that arbitration clauses must, under federal law established in the USAA, be viewed as '"separable"' from other portions of a contract [citation]; hence, fraud in the inducement relating to other contractual terms does not render the arbitration agreement unenforceable, even when it might justify rescission of the contract as a whole. By entering into the arbitration agreement, the parties established their intent **[*10]** that disputes coming within the agreement's scope be determined by an arbitrator rather than a court; this contractual intent must be respected even with regard to claims of fraud in the inducement of the contract generally. [P] Where, however, a party's apparent assent to a written contract is *negated* by fraud in the inception, there is simply no arbitration agreement to be enforced. As one Court of Appeal recently explained, *Prima Paint* does not require 'allegations directed specifically and solely at the agreement to arbitrate. *Prima Paint,* rather, requires some allegation [and, as we held earlier, evidence] from which it may be determined that the parties in fact did not intend to arbitrate the issues set forth in the pleadings. The allegation may be directed solely at the "making" of the agreement to arbitrate or, as recognized by the doctrine of fraud in the inception, it may be directed at the "making" of the contract as a whole.' [Citation.] [P] In the absence of a contrary agreement, parties to a predispute arbitration agreement are presumed to have intended arbitration of controversies, including allegations of fraud in the inducement of the contract generally, **[*11]** that may allow rescission or reformation of the contract or part of it. They cannot, however, have intended arbitration under a contract wholly void for fraud in its execution. We therefore conclude *Prima Paint* does not preclude the court from deciding claims of fraud in the execution of the entire contract. The same is true of California law under our decision in [*Ericksen, Arbuthnot, McCarthy, Kearney & Walsh, Inc. v. 100 Oak Street* (1983) 35 Cal.3d 312, 197 Cal. Rptr. 581], in which we explicitly distinguished cases where the party opposing arbitration '"denied ever agreeing to anything."' [Citation.]" (*Rosenthal, supra,* 14 Cal.4th at pp. 415-417, italics in original.)

Of course, in the matter before us, there is no claim of fraud, either in the inception or inducement. However, the more significant principle to be gleaned from the foregoing analysis is that an allegation that the version of the agreement proffered by Brown never came into existence as a contract because there was never mutual assent to its terms is one for the court, not the arbitrator, to consider. (*Camping Constr. Co. v. District Council* (9th Cir. 1990) 915 F.2d 1333,1340 **[*12]** ["The court must determine whether a contract ever existed; unless that issue is decided in favor of the party seeking arbitration, there is no basis for submitting any question to an arbitrator." (Italics omitted.)].)

Brown relies upon *Teledyne, Inc. v. Kone Corp.* (9th Cir. 1989) 892 F.2d 1404 (*Teledyne*), for the proposition that the question of a contract's existence is for the arbitrator, not the court. In *Teledyne,* the parties signed a document entitled "'DRAFT (to be finalized by KONE legal department).'" Teledyne raised contractual claims in its complaint. Kone, the defendant, moved to compel arbitration under the terms of the signed document. However, as a defense to the action, Kone contended that no final, valid contract existed. The trial court granted Kone's motion to compel arbitration. (*Id.* at p. 1406.) The appellate court affirmed, holding that a trial court may consider only those challenges to the arbitration clause itself, not those to the making of the contract as a

whole. (*Id.* at pp. 1410-1411.) Because Teledyne was not challenging the arbitration clause itself, the appellate court found Teledyne's position **[*13]** that the trial court, rather than the arbitrator, must determine whether a contract exists to be "absurd": "The district court could grant Teledyne relief on the contract only if it finds that the 1986 Draft was finalized. But if the 1986 Draft were final and valid, the arbitration provision would be valid as well since it has not been the subject of any independent challenge. And if the arbitration provision were valid, Teledyne's claims would not belong in federal court in the first place." (*Ibid.*)

In *Sandvik AB v. Advent Intern. Corp.* (3rd Cir. 2000) 220 F.3d 99 (*Sandvik)*, the plaintiff raised contractual claims in its suit but resisted arbitration. The defendant moved to compel arbitration under a written agreement that it simultaneously contended was not binding because its signator lacked authority to bind it. Thus, though the legal ground upon which the defendant contended no contract existed was different than that raised by Kone in *Teledyne,* the positions of the plaintiffs-Teledyne and Sandvik-were the same, i.e., they each raised contractual claims but denied that the arbitration clause contained within the written agreement required arbitration **[*14]** of the question of the contract's existence. The *Sandvik* court found no absurdity in this position: "If the court declares that such a contract existed or otherwise finds that the arbitration clause is binding, arbitration would then be ordered on all issues arising within the scope of the abritration clause . . . ." (*Id.* at p. 111.) The court went on to note: "Insofar as [the plaintiff's] position leads to an 'absurdity,' it is no greater than the one urged by [the defendant,] for there is something odd about referring this matter to arbitrators without a definitive conclusion on the issue whether an agreement to arbitrate actually existed. Were we to order the District Court to compel arbitration and were the arbitrators ultimately to decide that [the signator's] signature did not bind Advent, they will have effectively decided that they had no authority to arbitrate the dispute. Such a ruling would, however, allow the arbitrators to determine their own jurisdiction, something that is not permitted in the federal jurisprudence of arbitration, for the question whether a dispute is to be arbitrated belongs to the courts unless the parties agree otherwise. **[*15]** [Citations.]" (*Ibid.*)

The court in *Sandvik* concluded that "when the very existence of such an agreement is disputed, a district court is correct to refuse to compel arbitration until it resolves the threshold question of whether the arbitration agreement exists." (*Sandvik, supra,* 220 F.3d at p. 112.) In doing so, the court looked to *Three Valleys Mun. Water Dist. v. E.F. Hutton* (9th Cir. 1991) 925 F.2d 1136 (*Three Valleys*), in which the question presented was whether the trial court or the arbitrator determined whether a valid contract existed, specifically whether the parties' representatives who signed the contract had authority to do so. The appellate court rejected the contention that *Prima Paint* required an arbitrator to resolve whether a valid contract had come into existence: "[W]e read *Prima Paint* as limited to challenges seeking to *avoid* or *rescind* a contract-not to challenges going to the very existence of a contract that a party claims never to have agreed to. A contrary rule would lead to untenable results. Party A could forge party B's name to a contract and compel party B to arbitrate the question of the **[*16]** genuineness of its signature. . . . [P] . . . If the dispute is within the scope of an arbitration agreement, an arbitrator may properly decide whether a contract is 'voidable' because the parties have agreed to arbitrate the dispute. But, because an 'arbitrator's jurisdiction is rooted in the agreement of the parties,' a party who contests the making of a contract containing an arbitration provision cannot be compelled to arbitrate the threshold issue of the *existence* of an agreement to arbitrate. Only a court can make that decision." (*Three Valleys, supra,* at pp. 11401141, italics in original, fn. & citations omitted.)

The *Three Valleys* court, too, was confronted with *Teledyne* and distinguished it on the basis that Teledyne could not avoid the arbitration clause in the contract because it had raised contractual claims in its complaint and had not made a separate challenge to the making of the arbitration clause. (*Three Valleys, supra,* 925 F.2d at p. 1142; see *Rosenthal, supra,* 14 Cal.4th at p. 416, fn. 9.) Here, ***Frog Creek*** has denied the existence of the contract as proffered by Brown in its motion to compel arbitration, and ***Frog*** **[*17]** ***Creek*** has made a separate challenge to the arbitration clause as found in that version. Thus, we find nothing absurd or anomalous in ***Frog Creek***'s position. [4]

Brown also relies upon *Republic of Nicaragua v. Standard Fruit Co.* (9th Cir. 1991) 937 F.2d 469, 477-479, **[*18]** in which the appellate court held that the trial court erred in first determining whether the memorandum signed by the parties was in fact a contract. To that extent, it distinguished *Three Valleys* as a case in which the trial court properly was to determine the authority of the signators to an agreement, not whether an agreement signed by those with authority was a contract. Finding little distinction, we believe *Three Valleys*

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[4] In *Microchip Technology Inc. v. U.S. Philips Corp.* (Fed. Cir. 2004) 367 F.3d 1350, the plaintiff sued on a contract claiming to be the successor in interest to the original signator but opposed the defendant's motion to compel arbitration under the terms of the contract. The trial court denied the motion to compel pending resolution of the question of whether the plaintiff was a successor in interest under the agreement. (*Id.* at pp. 1353-1354.) The appellate court affirmed. Rejecting the reasoning of *Teledyne*, the court found no requirement that there be an independent challenge to the arbitration clause or that there be no contractual claims in order for the plaintiff to avoid arbitration of the question of the contract's existence. (*Id.* at p. 1358.)

to be better reasoned.

We turn to general principles of California contract law in order to determine whether a contract existed here. (*Marcus & Millichap Real Estate Investment Brokerage Co. v. Hock Investment Co.* (1998) 68 Cal.App.4th 83, 89.) Because the evidence on this point consists of documents and written declarations, we review the issue de novo. (*Ibid.*)

A binding contract is not formed unless the terms of an offer are met ″exactly, precisely and unequivocally″ by the acceptance. (*Panagotacos v. Bank of America* (1998) 60 Cal.App.4th 851, 855 (*Panagotacos*).) Drazen's interlineations on behalf of ***Frog Creek*** constituted a counteroffer, not an acceptance. Drazen made clear that ***Frog Creek***'s acceptance **[*19]** was contingent upon the new terms. There is no evidence that Brown ever accepted this counteroffer. Indeed, the evidence that Brown was still disputing the amended landscaping cost a year and a half later is to the contrary. In *Panagotacos, supra*, the trial court considered whether the plaintiffs had a valid real estate purchase contract. There, the original offer was made by the seller in a letter and included a condition that the funds be paid in Germany. Plaintiffs responded by letter, purporting to accept the offer but indicating that payment would be made in Greece. The sellers responded that the place of payment was essential and that there was, as a result, no agreement. The trial court correctly concluded that no contract existed because, even though the essential terms of the contract had been set forth in the offer, the plaintiffs' letter was a counteroffer, not an acceptance. (*Id.* at pp. 855-856.) The case before us is analogous to *Panagotacos*. Here, no contract resulted from Brown's offer contained in its version of the agreement.

Having concluded that Brown's version of the agreement did not constitute a contract, it necessarily follows **[*20]** that the trial court's denial of Brown's motion to compel arbitration was correct because that motion was based on Brown's version of the agreement. The trial court was not asked to rule upon the question of whether ***Frog Creek***'s version of the agreement was a binding contract and whether the parties were required to arbitrate pursuant to that version of the agreement. Consequently, we take no position on those questions here.

Brown argues that ***Frog Creek*** should be estopped from denying the existence of the contract for a number of reasons: (1) it was ***Frog Creek*** that requested mediation, which was the precursor to arbitration under the contract; (2) in its complaint, ***Frog Creek*** alleged contractual causes of action and attached its copy of the document to the complaint; (3) ***Frog Creek*** had already paid over eight million dollars to Brown for services rendered under the contract; and (4) ***Frog Creek*** had issued change orders to the original agreement.

We are unpersuaded by any and all of these circumstances. As noted, ***Frog Creek*** has not denied the existence of a valid construction contract. None of the circumstances recited by Brown is inconsistent with ***Frog Creek***'s overall litigation **[*21]** position. [5]

[*22] II. DISPOSITION

The judgment is affirmed.

REARDON, J. [*]

We concur.

SIMONS, Acting P.J.

GEMELLO, J.

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[5] In so resolving the case, we need not consider Frog Creek's contention that Brown, as a licensed contractor, is not permitted to rely upon the terms of a written agreement that does not comply with Business and Professions Code section 7164 in that no single written agreement exists and Brown did not provide a written agreement to Frog Creek before commencing work. This section was designed to protect consumers in dealings with contractors. (*Arya Group, Inc. v. Cher* (2000) 77 Cal.App.4th 610, 614.) Ironically, compliance with the section may have assisted Brown in its efforts to compel arbitration under its version of the agreement.

Frog Creek has asserted the validity of its version of the agreement by alleging contract-based claims in its verified cross-complaint. Based upon the comments of counsel at oral argument, if Frog Creek's version of the agreement is upheld, we anticipate Frog Creek's separate challenge to the enforceability of the arbitration clause found in that version.

[*] Judge of the Superior Court of Alameda County, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.