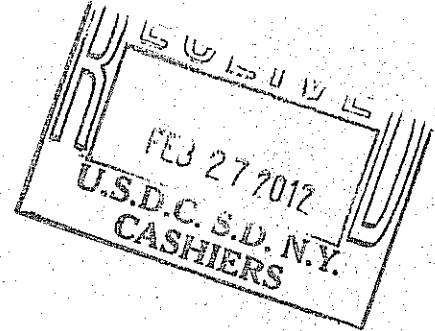


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**JUDGE KAPLAN**

**12 CIV 1434**

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**UNITED STATES DISTRICT COURT  
SOUTHERN DISTRICT OF NEW YORK**

<b>TOTO, INC.,</b>	)	
	)	Case No. _____
<b>Plaintiff,</b>	)	
	)	
v.	)	<b>COMPLAINT FOR BREACH OF</b>
	)	<b>CONTRACT; BREACH OF THE</b>
	)	<b>IMPLIED DUTY OF GOOD FAITH AND</b>
<b>SONY MUSIC ENTERTAINMENT,</b>	)	<b>FAIR DEALING; an ACCOUNTING;</b>
	)	<b>and, DECLARATORY JUDGMENT</b>
	)	
<b>Defendant.</b>	)	
	)	<b><u>DEMAND FOR JURY TRIAL</u></b>

Plaintiff Toto, Inc. ("Toto"), by and through its attorneys, for its Complaint against the Defendant named above alleges as follows:

**Parties**

1. Plaintiff Toto is a California Corporation with its principal place of business at 16830 Ventura Boulevard; Suite 501; Encino, California 91436.

2. Defendant Sony Music Entertainment (“Sony”) is a subsidiary of Sony Corporation of America, which is a New York Corporation. Sony’s principal place of business is located at 550 Madison Avenue, New York, NY 10022.

### **Jurisdiction and Venue**

3. The jurisdiction of this Court is based upon 28 U.S.C. § 1332 as there is complete diversity of citizenship between the parties, and the amount in controversy exceeds \$75,000.00 exclusive of interest and costs. This action for declaratory judgment is brought pursuant to 28 U.S.C. § 2201 which is within the exclusive jurisdiction of federal courts pursuant to 28 U.S.C. § 1331. Venue is proper in the District pursuant to 28 U.S.C. §§ 1391 and 1400(a).

4. Personal jurisdiction over Sony is proper in this Court on the grounds that (a) Sony transacts business in the State of New York; (b) Sony’s wrongful conduct, alleged herein, occurred in the State of New York and in this District; and, (c) the Recording Agreements, as defined below, that are the subject of this action were entered into in this District.

5. Venue is proper in this District pursuant to 28 U.S.C. § 1391(a)(c).

### **Factual Allegations**

6. On or about December 10, 1977, Toto entered into a recording agreement with Sony’s predecessor CBS Records, Inc. (Sony and its predecessor are collectively referred to as “Sony” hereinafter). Toto also entered into subsequent recording agreements with Sony on or about January 27, 1983, and May 10, 1993. Between 1977 and 2003, Toto and Sony entered into other agreements amending and/or supplementing these recording agreements. (collectively the “Recording Agreements”).

7. Pursuant to and during the terms of the foregoing Recording Agreements, Toto caused certain “master” recordings of musical performances (the “Masters”) to be made and delivered to

Sony, which Masters Sony had agreed to manufacture, distribute, sell, and license for sale and distribution in various configurations.

8. In consideration of Toto's performance under the Recording Agreements, Sony agreed to pay Toto under a certain royalty structure and to account to Toto under that royalty structure. In order to ensure Sony correctly accounted to and paid Toto, the Recording Agreements gave Toto the explicit right to inspect Sony's books and records through an audit procedure. In conjunction with this right to audit Sony's books and records, Sony agreed to allow Toto access to "the books and records which relate to [Toto] and which are necessary to verify the accuracy of the statement or statements" provided by Sony.

9. Since entering into the first of the Recording Agreements on December 10, 1977, and despite its obligations under the Recording Agreements, Sony has consistently failed to properly account to and pay Toto under the royalty structure set forth in the Recording Agreements.

10. On or about June 7, 2006, Toto and Sony entered into a Settlement Agreement settling most of Toto's royalty disputes through December 31, 2004.

11. During the period beginning on January 1, 2005 and continuing through the present, Sony has continued to fail to properly account to and pay Toto under the royalty structure set forth in the Recording Agreements.

12. Pursuant to its audit rights under the Recording Agreements, Toto, through an accounting firm, performed an audit of Sony's books and records regarding Sony's accountings and payments to Toto for the period January 1, 2006 through June 30, 2008 (the "Audit").

13. On or about March 16, 2010, Toto provided Sony with the results of the Audit, thereby providing notice of Sony's breach of the Recording Agreements. On or about August 10, 2010,

Sony responded to the Audit by falsely claiming it had overpaid Toto \$189,661 during the period in question.

14. On October 7, 2011, Toto and Sony entered into a tolling agreement which allowed suit over the claims of the Audit to be filed up to and including December 31, 2011. On December 6, 2011, Sony agreed to extend that tolling agreement up to and including March 31, 2012.

15. The Audit shows Sony has incorrectly calculated the number of products Toto sold, has incorrectly categorized those products, and has incorrectly paid Toto for products for which it has accounted, for total underpayments in excess of \$500,000.

16. During the Audit, Sony failed to provide documents supporting its adjustments, take-on balances, and period-beginning balances for the accounting periods beginning on January 1, 2006. Sony's failure to provide the requested documentation left Toto without the ability to verify or determine the accuracy of \$918,596.18 in so-called "miscellaneous adjustments." Eventually, backup documentation regarding these adjustments was provided. However, this documentation showed that Toto was underpaid by at least \$43,561.79. This \$43,561.79 underpayment is the direct result of Sony using a shortcut to recalculate foreign royalties instead of reprocessing and recalculating royalties. Sony's incorrect calculations have continued following the Audit, with Sony arguing it has overpaid Toto by \$18,357.35. Further, Sony has improperly attempted to recoup this amount which is not due Sony.

17. In addition to the foregoing underpayments, Sony has also failed to accurately make both domestic and foreign royalty calculations under the Recording Agreements.

18. For domestic sales of the Masters, Sony has failed to support the base prices used in calculating royalties for Phonograph Records sold resulting in underpayments to Toto. Sony has also incorrectly and improperly taken deductions from the royalty calculations. For instance,

Sony took distribution channel deductions, such as television advertising deductions, which are not supported by ad campaign documentation and are therefore not allowed under the terms of the Recording Agreements. During the Audit, Sony failed to provide books or records reflecting the base price used for calculations for the 2007 and 2008 royalty periods; however, the books and records provided show that Toto has been underpaid by a minimum of \$134,325.89 for domestic sales based on Sony's use of incorrect base prices and taking incorrect and improper deductions. Sony's actions in this regard have breached its duty to properly account to and pay Toto, as well as its duty to allow Toto to conduct a fair and accurate audit. In fact, Sony admits it has breached the Recording Agreements by underpaying Toto under its domestic royalty calculations. However, Sony has only agreed to \$2,278.00 of the at least \$134,325.89 actually owed.

19. Both Toto and Sony agree Sony used incorrect calculations in paying Toto for the sale of foreign Phonograph Records. Both Toto and Sony agree that Sony overpaid Toto based on Sony's incorrect foreign royalty calculation. However, in determining the amount of overpayment, Sony has used an incorrect formula. Sony has attempted to use a price based on Sony's actual sale prices instead of the Suggested Retail Price, which is controlling under the Recording Agreements. Further, Sony has taken incorrect deductions in making its foreign royalty calculation. Sony has actually overpaid Toto under the foreign royalty calculation covered by the Audit in the amount of \$49,344.42. Sony incorrectly claims the overpayment is \$107,884.00. This incorrect calculation has resulted in Sony attempting to recoup, from Toto, an amount greater than what is recoupable under the Recording Agreements.

20. The Audit also showed that Sony failed to pay Toto an additional \$62,173.58 for products sold incorporating the Masters, but not properly listed in the normal royalty accounting system.

Sony has since made a partial payment on this amount. However, Toto is still owed a minimum of \$49,499.58 for products Sony failed to properly list and/or match-up in its royalty accounting system. Sony has attempted to justify its actions by showing supposed accountings for these products with comparisons of Sony's SAP and Core reports. However, this justification is unsupported and improper. Sony's failure to list these products in its normal retail system is a violation of its duty to accurately account to Toto and is a failure to provide the necessary documentation in order for Toto to be able to conduct a proper audit as contemplated by the Recording Agreements. Sony admits it is still in breach of the Recording Agreements, but incorrectly limits its breach to merely \$697.00.

21. In addition to these failures to correctly account and pay claims, the Audit revealed that Sony failed to properly account to and pay Toto for Masters leased to third-party Music Download and Mastertone Providers, such as iTunes (Apple), eMusic, amazon.com, Verizon Wireless and others. Music Download and Mastertone Providers are third-parties that licensed (or "leased" in Sony's parlance,) the Masters from Sony and then distributed downloads and mastertones to end users on computers, cell phones, or other devices.

22. The Recording Agreements state, "In respect of any Master Recording leased by [Sony] to others for their distribution of Phonograph Records in the United States [Sony] will pay [Toto] 50% of [Sony's] net receipts."

23. Under the terms of the Recording Agreements, music downloads, mastertones, and ringtones are "Phonograph Records."

24. After January 1, 2005, Sony leased the Masters to third party Music Download and Mastertone Providers, so that those third party Music Download and Mastertone Providers could distribute music downloads, mastertones, and ringtones to the public. Sony received monies for

this leasing and continuously and persistently failed to account to and pay Toto the 50% of net receipts due to it pursuant to the terms of the Recording Agreements.

25. Instead, between January 1, 2005 and present, Sony systematically accounted to and paid Toto for the Masters leased to third parties, including third party Music Download and Mastertone Providers at lower royalty rates, under provisions of the Recording Agreements, which are applicable only to Phonograph Records sold by Sony, and are not applicable to the leasing of the Masters. Further, Sony took unwarranted and unallowed deductions from the small amount of royalties it actually paid to Toto.

26. On March 16, 2010, Toto provided Sony with the Audit specifically informing Sony of its wrongful method of paying Toto in regards to Masters leased to Music Download and Mastertone Providers.

27. In response to the Audit, Sony stated that a sales provision of a 1986 amendment to the Recording Agreements applied to music downloads, mastertones, and ringtones distributed and/or sold by Music Download and Mastertone Providers. In support of this position, Sony stated, "iTunes and other DSPs [Digital Service Providers] and ringtone providers do not license content from Sony for sale as permanent downloads. Sony sells tracks directly to consumers through DSPs, as Sony's agents, or the DSPs purchase tracks wholesale and resell them to consumers."

28. Sony's response to Toto's Audit is both factually and legally incorrect. Sony leases Masters to Music Download and Mastertone Providers; Sony does not sell music downloads, mastertones, and ringtones directly to consumers. Instead, Sony leases Masters to Music Download and Mastertone Providers and those Music Download and Mastertone Providers then reproduce the Masters to create music downloads, mastertones, and ringtones which those party

licensees sell directly to consumers. Sony's position was explicitly rejected in *F.B.T. Prods., LLC v. Aftermath Records*, 621 F.3d 958 (9th Cir. 2010).

29. Sony also asserts that it is able to take certain deductions from the royalties paid on music downloads, mastertones, and ringtones distributed or sold by Music Download and Mastertone Providers under a provision in the Recording Agreements (specifically, a 2002 Settlement Agreement and a 1986 Modification) providing for payment of royalties for so-called "audiophile" records. However, this Audiophile provision is not applicable to music downloads, mastertones, or ringtones leased to Music Download and Mastertone Providers.

30. The Audiophile provision is only applicable to sales by Sony or Sony's Principal Licensee.

31. Principal Licensee is a term of art which refers only to Sony's subsidiary or partner that manufactures and distributes phonorecords in a certain foreign territory in which Sony, itself, does not manufacture or distribute Phonograph Records.

32. Principal Licensees are a separate and distinct class from the type of third-party licensees that encompass Music Download and Mastertone Providers.

33. This distinction is readily apparent because Sony pays royalties on compact discs sold by its Principal Licensees under the Audiophile provision of the Recording Agreements, but pays royalties on compact discs sold by third-party licensees under the royalty method contained in the Masters leased provision of the Recording Agreements, described above in paragraph 23. Under the terms of the Recording Agreements, Toto is paid "50% of [Sony's] net receipts" for compact discs sold by third-party licensees. Toto is also entitled to be paid "50% of [Sony's] net receipts" for music downloads, mastertones, and ringtones derived from Masters leased to third-party Music Download and Mastertone Providers.



34. Sony's failure to correctly pay Toto for music downloads, mastertones, and ringtones derived from Masters leased to Music Download and Mastertone Providers has resulted in Sony underpaying Toto by at least \$199,856.16.

35. Following the Audit, instead of correcting this underpayment and agreeing to correctly account to and pay Toto, Sony has incorrectly claimed it overpaid Toto by \$63,016 for music downloads, mastertones, and ringtones derived from Masters leased to Music Download and Mastertone Providers. Sony has attempted to state it is entitled to recoup this \$63,016; however, that amount is not due to Sony. Further, Sony has continued to deny its obligation to properly account to and pay Toto for music downloads, mastertones, and ringtones derived from Masters leased to Music Download and Mastertone Providers.

36. For the period audited, Sony has failed to account for and pay Toto in excess of \$500,000. Upon information and belief, Sony's failure to properly account to and pay Toto continues in the royalty periods following the Audit which has and will continue to result in additional monetary damages not yet known to Toto.

37. Further, Sony's failure to timely pay Toto, as required by the Recording Agreements, has caused Toto to be deprived of the use of substantial funds causing additional financial harm.

38. In addition to Sony's failure to correctly pay Toto, Sony is currently attempting to improperly recoup more than \$175,000 from Toto which has the direct effect of preventing Toto from collecting more than \$175,000 it is owed. These failures have created a dispute in excess of \$605,516.65 with respect to Sony's breach of the Recording Agreements.

### **Claim I**

#### **Breach of Contract**

39. Toto realleges each and every allegation in paragraphs 1 through 38 as if fully set forth herein.

40. Toto and Sony have valid and enforceable contracts, the Recording Agreements.

41. Sony has failed to comply with the terms of the Recording Agreements, and failed to fulfill its obligations under the Recording Agreements, by failing to properly account to and pay Toto royalties for sales of the Masters. Sony's failures include, but are not limited to, incorrectly calculating products sold, incorrectly paying Toto based on products sold, failing to allow Toto a full and fair opportunity to conduct an audit, attempting to recoup monies not owed to Sony, and failing to account to and pay Toto fifty percent (50%) of Sony's net receipts from its leasing of the Masters to third parties, including Music Download and Mastertone Providers.

42. By reason of the foregoing and other acts not presently known by Toto, Sony has knowingly and materially breached its contractual obligations to Toto under the Recording Agreements.

43. Sony's material breach of the Recording Agreements is the legal cause of substantial damage to Toto for which Toto seeks monetary damages in an amount to be determined at the time of trial, which upon information and belief is in excess of \$605,000.

## **Claim II**

### **Breach of the Duty of Good Faith and Fair Dealing**

44. Toto realleges each and every allegation in paragraphs 1 through 43 hereof as if fully set forth herein.

45. Toto and Sony have valid and enforceable contracts, the Recording Agreements.

46. Toto has performed all its obligations under the Recording Agreements.

47. Sony, by and through its conduct and actions described in the Complaint, and by other actions not presently known by Toto, wrongfully withheld the benefits of the Recording Agreements from Toto. Such actions by Sony frustrated the purpose of the Recording Agreements.

48. Sony's actions in wrongfully withholding the benefits of the Recording Agreements from Toto and frustrating the purpose of the Recording Agreements is the legal cause of substantial damage to Toto for which Toto seeks monetary damages in an amount to be determined at the time of trial.

### **Claim III**

#### **Accounting**

49. Toto realleges each and every allegation in paragraphs 1 through 48 hereof as if fully set forth herein.

50. Toto, due to the wrongful acts of Sony, is entitled to a full accounting by Sony of amounts relating to the royalties received under the Recording Agreements, whereby Toto may determine the revenues, profits, and royalties rightfully belonging to Toto and wrongfully gained by Sony.

### **Claim IV**

#### **Declaratory Judgment**

51. Toto realleges each and every allegation in paragraphs 1 through 50 hereof as if fully set forth herein.

52. Pursuant to 28 U.S.C. § 2201, this Court may declare the rights and other legal relations of any interested party seeking such declaration whether or not further relief is, or could be,

sought. Any such declaration shall have the force and effect of a final judgment or decree and shall be reviewable as such.

53. Toto seeks a declaration that, pursuant to the Recording Agreements, Sony is obligated to pay Toto fifty percent (50%) of Sony's net receipts derived from the leasing of the Masters to others for the manufacture and sale of Phonograph Records or for any other uses, including but not limited to the leasing of the Masters to Music Download and Mastertone Providers.

54. Sony denies the leasing of the Masters to Music Download and Mastertone Providers requires it to pay Toto fifty percent (50%) of Defendant's net receipts.

55. Sony continues to lease the Masters to Music Download and Mastertone Providers and receive payment from Music Download and Mastertone Providers, but, on information and belief, continues to account to Toto for these leases at a royalty rate that is less than fifty percent (50%) of Sony's net receipts from those leases.

56. By reason of the foregoing, there is a present controversy between Toto and Sony for which a declaratory judgment should be entered.

57. Toto has no adequate remedy at law.

#### **Prayer for Relief**

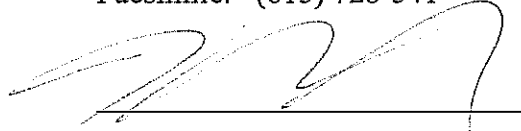
WHEREFORE, Toto prays for judgment against Sony as follows:

1. Compensatory damages in excess of \$605,000, the exact amount of which to be determined at the time of trial;
2. An Order requiring Sony to provide Toto with a full accounting;
3. An Order and Judgment declaring that the Recording Agreements require Sony to account to and pay Toto fifty (50%) of net receipts for leasing of the Masters, including leasing to Music Download and Mastertone Providers;

4. An award of actual and reasonable attorneys' fees and costs for services rendered to Toto in this action;
5. An award of pre- and post-judgment interest;
6. A trial by jury on all triable issues; and,
7. Such other and further relief as the Court deems just and proper.

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