



How *Fifty Shades of Grey* Is Redefining Texas Law

A court battle over royalties from the steamy E.L. James trilogy is changing the meaning of business partnerships.

BY JOHN G. BROWNING | FROM D CEO DECEMBER 2015

Within months of the eagerly anticipated release of the movie "Fifty Shades of Grey," drama of an entirely different sort was unfolding in a North Texas courtroom. At issue were royalties from the series of books by E.L. James that spawned the movie "Fifty Shades of Grey"—the original "Fifty Shades," plus "Fifty Shades Darker" and "Fifty Shades Freed." But instead of an erotic clash of wills between mysterious billionaire Christian Grey and young Anastasia Steele over the boundaries of their BDSM relationship, this drama pitted a former Mansfield elementary school teacher against an Australian national in a dispute that would help redefine what constitutes a partnership under Texas law.

It all began innocently enough in 2009, when Arlington resident Jennifer Pedroza and Amanda Hayward of Australia met online through a fan fiction website. The two became friends and decided to start a website of their own where writers could upload their own stories, blog, and discuss their work. By January 2010, The Writer's Coffee Shop was born, with Hayward working with authors on moving their work onto the site, Pedroza helping the writers with uploading and blogging, and another North Texan—Jennifer McGuire of Waxahachie—assisting with the site's graphics. Although The Writer's Coffee Shop initially subsisted on ad revenue, by the end of 2010 Pedroza and Hayward realized that publishing itself could generate income and decided to operate the site as a publishing house. In May 2011, the pair struck gold when The Writer's Coffee Shop obtained the rights to work by a former writer of "Twilight" fan fiction, Erika Leonard, writing under the pseudonym E.L. James. The Writer's Coffee Shop published James' "Fifty Shades of Grey" as an e-book and a print-on-demand full-length novel. The site went on to publish James' two sequels, "Fifty Shades Darker" (in September 2011) and "Fifty Shades Freed" (in January 2012). Pedroza was in charge of marketing for the site, and not only issued press releases and made speaking appearances to promote The Writer's Coffee Shop, but also filled book orders, packaging and mailing them from her Arlington home. By August 2011, Hayward purportedly brought in another Australian, Lea Dimovski, as a partner to assist with the burgeoning enterprise.

"Fifty Shades" became an online phenomenon. The Writer's Coffee Shop sold an estimated 250,000 copies of the e-book and shipped another 20,000 paperbacks to customers en route to winding up on The New York Times' best seller list. Major publishing houses clamored for the rights and, in March 2012, Random House emerged as the winner when it agreed to pay E.L. James and The Writer's Coffee Shop a lucrative advance plus future royalties. Although Hayward presented the offer to Pedroza and McGuire (who both approved it), Hayward herself signed the contract and, according to Pedroza, never provided the others with either the contract itself or its full terms. Throughout 2012, Pedroza continued to promote the "Fifty Shades" trilogy at book expos and publishing events all over the country, even as she began hearing disturbing things from Hayward.

According to Pedroza, The Writer's Coffee Shop had a written partnership agreement—it reflected that each of the four partners had a 25 percent interest in the business—and, although it hadn't been signed, they always viewed themselves as partners and conducted their business as a partnership. For example, in March 2011 The Writer's Coffee Shop (with Pedroza as a general partner) filed a U.S. tax return of partnership income with the IRS. In 2012, the company operated with two bank accounts, one in the U.S. and one in Australia, with payments for book sales from companies like iTunes and Amazon going into the American account, out of which Pedroza would issue royalty payments to authors. But according to Pedroza, after the deal with Random House closed, all payments from Random House went directly to Australia. Even more troubling, she alleges, is that Hayward convinced her that the business was in bad shape financially and needed to be restructured as a new and separate company called TWCS, with Pedroza and McGuire signing "service agreements" with the new entity. Under the terms of this agreement, Pedroza would receive a one-time payment of \$100,000 plus a \$5,000 monthly salary as "marketing director" for TWCS, although there was a provision making Pedroza's employment terminable without cause on seven days' notice.

According to Pedroza, when she expressed concern about the termination clause, Hayward responded via email: "I would NEVER do that to you even if we fall out and have a huge fight. Out of respect to you and our friendship. I swear on my daughters lives..." and dismissed the provision as something "the lawyers" insisted on. In November 2013—one day, Pedroza maintains, after TWCS/Hayward received a third royalty payment from Random House that wasn't disclosed or shared with her erstwhile partner—Hayward terminated Pedroza.

Pedroza needed legal help, and she turned to a uniquely qualified lawyer, Michael Farris. In addition to being an accomplished trial lawyer and of counsel at Dallas' Vincent Serafino Lopez Jenevein, Farris is no stranger to the ins and outs of the publishing world. He's the author of five novels and two nonfiction books and, since 2002, has operated the Farris Literary Agency, representing authors in their dealings with publishing houses. Farris and

Pedroza filed a lawsuit against Hayward and TWCS Operations Pty. Ltd. in May 2014 in the 153rd Judicial District Court in Tarrant County. Farris called the chain of events leading to the lawsuit a story that “has all the makings of a great novel: ‘Fifty Shades of Greed’ by Amanda Hayward.”

In the lawsuit, Pedroza asked the court to declare that a partnership existed, and that Hayward’s actions in forming new and separate companies in Australia didn’t dissolve or “convert” the original partnership. She also sued Hayward for breaching her partnership and fiduciary duties and fraud and fraudulent inducement, and obtained a temporary injunction to keep Hayward from enforcing the service agreement or from transferring or disposing funds received under the Random House deal. In addition, she also sought an accounting of all the monies that had been received. Hayward and TWCS Operations Pty. Ltd., through their lawyer (Jones Day’s Robert Kantner) counterclaimed, arguing that Pedroza had breached her service agreement by suing. In addition, the defendants argued that there was no signed written contract memorializing the partnership.

To refute this, and to document what he calls “a story about misplaced trust and betrayal,” Farris argued that Texas law recognizes, in the absence of a signed agreement, the doctrine of partnership by conduct. Simply put, where two or more individuals express an intent to be partners in a business, participate in the control of that business, agree to share in its losses, and agree to contribute money toward the business, these actions can speak just as loudly as the written words on a signed contract. And Farris had a field day pointing out the many instances in which Hayward actually referred to Pedroza as “one of the partners” or “one of the founders” of The Writer’s Coffee Shop, as well as the myriad actions Pedroza took as a partner (like filing a partnership tax return or getting an Employer Identification Number). Following a five-day trial in February (just before the release of the movie version of “Fifty Shades of Grey”), the jury found in favor of Jennifer Pedroza, ruling that The Writer’s Coffee Shop was indeed a partnership, that Pedroza was a 25 percent partner in it, and that she was entitled to recover 25 percent of The Writer’s Coffee Shop’s profits due to Hayward’s fraud, along with her attorney’s fees.

But just what that 25 percent stake would amount to, in the wake of the “Fifty Shades” movie’s sensational success, has proven to be a tougher question to answer. Judge Susan McCoy held off on signing a final judgment pending determination of what the royalties amount to. After forensic accountants on both sides came up with similar calculations that Pedroza’s 25 percent interest would be worth approximately \$10.7 million (based on more than \$41 million in royalties to The Writer’s Coffee Shop), Judge McCoy ordered the defendants to deposit at least \$10 million into the registry of the court. Complicating matters is the contention by Hayward’s appellate counsel David Keitner that his client doesn’t have \$10 million in cash. The biggest asset listed in court records is Hayward’s home in the affluent Sydney suburb of Doral, and Farris has expressed concerns that Hayward spent much of the money “for her own personal benefit.”

A final chapter may yet be written. Hayward has sought mandamus relief from Judge McCoy’s order from the Fort Worth Court of Appeals, and the final judgment itself will undoubtedly be appealed. Or, to put it into terms more familiar to fans of the steamy “Fifty Shades” series, Hayward refuses to submit to the judge’s ruling or to be bound by the jury’s finding unless she’s ultimately restrained by the appellate courts. Meantime, Farris says there are lessons to be learned from this for entrepreneurs everywhere. Although you “really should get things in writing,” he cautions, “whether you consider yourself a partnership or not,” actions can speak louder than words, and “there are going to be consequences.”

