GARY E. KLAUSNER (SBN 69077)
gek@lnbyb.com
JEFFREY S. KWANG (SBN 288239)
jsk@lnbyb.com
LEVENE, NEALE, BENDER, YOO & BRILL L.L.P.
10250 Constellation Boulevard, Suite 1700
Los Angeles, California 90067
Telephone: (310) 229-1234

KEVIN D. RISING (SBN 211663)
kevin.rising@btlaw.com
RACHEL LERMAN (SBN 193080)
rachel.lerman@btlaw.com
JOEL R. MEYER (SBN 247620)
joel.meyer@btlaw.com
BARNES & THORNBURG LLP
2029 Century Park East, Suite 300
Los Angeles, California 90067
Telephone: (310) 284-3880

Attorneys for Strategic Global Management, Inc.; Kali P. Chaudhuri, M.D.; KPC Healthcare Holdings, Inc.; KPC Health Plan Holdings, Inc.; KPC Healthcare, Inc.; and KPC Global Management, LLC

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA - WESTERN DIVISION

In re:

VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*

Debtors and Debtors in Possession,

☒ Affects All Debtors
☐ Affects Verity Health System of California, Inc.
☐ Affects O'Connor Hospital
☐ Affects Saint Louise Regional Hospital
☐ Affects St. Francis Medical Center
☐ Affects St. Vincent Medical Center
☐ Affects Seton Medical Center
☐ Affects O'Connor Hospital Foundation
☐ Affects Saint Louise Regional Hospital Foundation
☐ Affects St. Francis Medical Center

Case No. 2:20-CV-00613-DSF

Related to District Court Appeals: Case Nos.: 2:19-cv-10352-DSF; 2:19-cv-10354-DSF; and 2:19-cv-10356-DSF)

Lead Chapter 11 Bankr. Case 2:18-bk-20151-ER

Jointly Administered With:

CASE NO.: 2:18-bk-20162-ER
CASE NO.: 2:18-bk-20163-ER
CASE NO.: 2:18-bk-20164-ER
CASE NO.: 2:18-bk-20165-ER
CASE NO.: 2:18-bk-20167-ER
CASE NO.: 2:18-bk-20168-ER
CASE NO.: 2:18-bk-20169-ER
CASE NO.: 2:18-bk-20171-ER
CASE NO.: 2:18-bk-20172-ER
CASE NO.: 2:18-bk-20173-ER
CASE NO.: 2:18-bk-20175-ER
CASE NO.: 2:18-bk-20176-ER
CASE NO.: 2:18-bk-20178-ER

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of Lynwood Foundation ☐ Affects St. Vincent Foundation ☐ Affects St. Vincent Dialysis Center, Inc. ☐ Affects Seton Medical Center Foundation ☐ Affects Verity Business Services ☐ Affects Verity Medical Foundation ☐ Affects Verity Holdings, LLC ☐ Affects De Paul Ventures, LLC ☐ Affects De Paul Ventures - San Jose Dialysis, LLC, Debtors and Debtors-in-Possession.	CASE NO.: 2:18-bk-20179-ER CASE NO.: 2:18-bk-20180-ER CASE NO.: 2:18-bk-20181-ER
VERITY HEALTH SYSTEM OF CALIFORNIA, INC., a California nonprofit public benefit corporation, ST. VINCENT MEDICAL CENTER, a California nonprofit public benefit corporation, ST. VINCENT DIALYSIS CENTER, INC., a California nonprofit public benefit corporation, and ST. FRANCIS MEDICAL CENTER, a California nonprofit public benefit corporation, SETON MEDICAL CENTER, a California nonprofit public benefit corporation, and VERITY HOLDINGS, LLC, a California limited liability company; and Plaintiffs, v. KALI P. CHAUDHURI, M.D., an individual, STRATEGIC GLOBAL MANAGEMENT, INC., a California corporation, KPC HEALTHCARE HOLDINGS, INC., a California corporation, KPC HEALTH PLAN HOLDINGS, INC., a California corporation, KPC HEALTHCARE, INC., a Nevada corporation, KPC GLOBAL MANAGEMENT, LLC, a California Limited Liability Company, and DOES 1 through 500, Defendants.	Adv. Case No. 2:20-ap-01001-ER **DEFENDANTS' REPLY IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS PLAINTIFFS' COMPLAINT** Date: TBD Time: TBD Judge: Hon. Dale S. Fischer

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I. INTRODUCTION

The motion filed by Defendants Strategic Global Management, Inc. ("SGM"), along with Non-SGM Defendants Dr. Kali P. Chaudhuri, KPC Healthcare Holdings, Inc., KPC Health Plan Holdings, Inc., KPC Healthcare, Inc., and KPC Global Management, LLC sets forth numerous grounds for dismissal of Plaintiffs' Complaint, including: (1) the Court lacks subject matter jurisdiction pending a final decision on the related appeals; (2) Plaintiffs' fail to state a claim because: (a) they failed to satisfy conditions precedent to closing the sale; (b) their fraud claim is barred by the litigation privilege and precluded by their own allegations; and (c) their "tortious breach" claim does not exist; and (3) their alter ego claims fail as a matter of law. Plaintiffs do not mount any actual defense to these arguments. Instead, they misrepresent the law and facts in an attempt to distract the Court.

II. THE COMPLAINT SHOULD BE DISMISSED FOR LACK OF SUBJECT MATTER JURISDICTION.

Because the consolidated appeals involve the same issues as the subsequently filed Complaint, the bankruptcy court, and now this Court, are divested of jurisdiction to adjudicate the adversary proceeding until a final decision is reached on appeal. Plaintiffs' arguments to the contrary are meritless.[1]

First, Plaintiffs argue that the divestiture rule is not jurisdictional *per se*. (Opp. 11.) So what? Divestiture is mandatory, regardless of whether it is characterized as jurisdictional or prudential. *Hamer v. Neighborhood Housing Servs. of Chicago*, 138 S.Ct. 13, 17-18 (2017). Next, Plaintiffs argue the relief sought in the stay motion and the motion to dismiss are "contradictory." Not so. Defendants sought to stay the adversary proceeding, based on the divesture rule, when the Complaint was filed. When a stay was denied, Defendants had to respond, and moved to dismiss under

[1] Plaintiffs do not dispute that the adversary proceeding "involve[s] aspects of the case that are the subject of the pending appeal." *Mercado-Guillen v. McAleenan*, 2019 WL 1995331, at *2 (N.D. Cal. May 6, 2019).

Rule 12(b)(1).[2] Now that both the adversary proceeding and the appeals are before this Court, it should either dismiss the Complaint or stay the adversary proceeding pending final resolution of the consolidated appeals.

III. PLAINTIFFS' CLAIMS FAIL AS A MATTER OF LAW

A. Plaintiffs' Claims All Fail Because They Cannot Establish They Satisfied § 8.7 of the APA.

Plaintiffs were entitled to demand that SGM close the sale only after they had satisfied all conditions precedent to closing, including APA § 8.7, which required Plaintiffs to enter into a "settlement agreement" with DHCS permitting transfer of their Medi-Cal provider agreements to SGM, while releasing and discharging SGM from any liability for any claims against Plaintiffs. Plaintiffs themselves concede that, as of November 19, 2019, the date they asserted that "all conditions" to closing had been met, they had no agreement with DHCS. (Opp. 21:13-16); (Compl. ¶ 77.)

Plaintiffs nonetheless contend they "materially" complied with APA § 8.7, because: (1) two court orders, entered May 2 and October 11, 2019, "afforded equal or greater protection to SGM than any settlement could have" (Opp. 20),[3] and (2) Plaintiffs were engaged in negotiations with DHCS that ultimately led to a stipulation, executed on December 9, 2019, four days after the date by which they demanded SGM close the sale. (Opp. 21.) Plaintiffs' "material compliance" arguments contradict the APA, basic principles of contract law, and common sense.

The Debtors' *post-hoc* rationalization that they "materially complied" with

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[2] Local bankruptcy rule (LBR) 9013-1(l), is irrelevant. A local bankruptcy rule cannot supplant the divestiture rule. Further, the rule applies only when a motion to dismiss was previously denied. LBR 9013-1(l).

[3] Plaintiffs continue to rely on the bankruptcy court's November 18 and 27 orders, which are pending appeal in this Court. The bankruptcy court itself told Plaintiffs these orders should be given no effect in this litigation, which was acknowledged by Plaintiffs' counsel. (See Suppl. RJN, Ex. V at 29-31.) While defending the Bankruptcy Court's ruling, Plaintiffs' counsel even stated that he did not see how the orders "could be used for virtually any purpose." (*Id.* at 32.) Yet Plaintiffs refer to these orders throughout their Opposition. *See e.g.*, (Oppos. 21:2-7; 19:11-13.) This Court should disregard all such references.

APA § 8.7 by virtue of the two court orders fails for at least three reasons. First, § 8.7 requires a "settlement agreement," not court orders. SGM was entitled to a document executed by DHCS that released and discharged SGM from any claims based on Plaintiffs' liability to DHCS (including past claims amounting to $80 million). SGM did not bargain for the opportunity to argue that it was released from liability by a court order, should DHCS attempt to enforce such claims against SGM.

Second, the orders do not provide "greater or equal protection" than the settlement required by § 8.7. Plaintiffs' quotes from the memorandum decision are inapposite, because a memorandum is not a court order and because the memorandum decision was superseded by the October 11 order itself. That order expressly reserved DHCS' recoupment rights against the parties, so it did not satisfy the "full satisfaction, discharge and release" requirement of § 8.7. In any event, as of the December 5 closing date, DHCS had already appealed the October 11 order, making it non-final.

Plaintiffs' reliance on the May 2 sale order is likewise unavailing. That order, which generally provided for assets to be transferred to SGM free and clear of liens, expressly reserved for future resolution all issues regarding the transfer of the Medi-Cal provider agreements to SGM, including DHCS' recoupment rights: "Nothing in this Sale Order shall apply to Medical Provider Agreements until and unless there is a court order approving a settlement between the Debtor and DHCS or a court order resolving the DHCS' [sale] objection." (Opp. RJN Ex. B.) Plaintiffs thus cannot reasonably argue that DHCS' recoupment rights were extinguished by the sale order.

Next, Plaintiffs did not "materially comply" with § 8.7 by holding discussions with DHCS. Plaintiffs assert (citing only the unsworn statements of their counsel at a November 26 hearing) that they reached a "settlement agreement in principal with DHCS on November 22." (Opp. 21:8-10.) But they never produced any evidence, nor was any evidence cited in the Complaint, of an agreement or the terms of any such agreement. Indeed, an "agreement in principle" is well known legal speak for

something that is not yet a binding agreement. If Plaintiffs believed they had a binding agreement, they would have said so. SGM was not required to close based on a lawyer's unsubstantiated statement about an "agreement in principle."

Remarkably, Plaintiffs assert that "the APA did not require a written agreement or a Court approved agreement" to comply with §8.7, so that "an oral agreement" could satisfy § 8.7. (Opp. 21:8-16). Not so; the APA requires an agreement executed by DHCS.

In addition to not being pled in their Complaint, Plaintiffs' argument that SGM should have been prepared to close at some unspecified date after their scheduled December 5 closing date, when they might eventually reach an agreement with DHCS, is also meritless. Plaintiffs never notified SGM of the December 9 stipulation with DHCS, or asked SGM to close the sale after that. The APA did not require SGM to be prepared to close at an unspecified future date, in the absence of a proper notice to close following Plaintiffs' failure to satisfy all closing conditions. Plaintiffs' assertion that SGM should have closed the sale after December 9, without a new notice or a request to close, is baseless.

Plaintiffs' own conduct further undermines their argument. On December 5, Plaintiffs notified SGM it was in breach because it did not close the sale on that date. Plaintiffs did not state or imply that SGM would have another opportunity to close, or be obligated to close at another date. Next, on December 6, 2019, Plaintiffs filed an "Emergency Motion" for an OSC re contempt based on SGM's failure to close on December 5 in which they requested authority to terminate the APA. On December 17, Plaintiffs terminated the APA effective December 27, based on SGM's failure to close on December 5. Plaintiffs then filed a Complaint alleging breach of contract based on SGM's failure to close on December 5. (Compl. ¶ 97.) To suggest now that SGM was required to stand by and wait for a new closing demand (which never materialized) while under attack from Plaintiffs for breaching the APA is ludicrous.

Plaintiffs' claim that the December 9 stipulation with DHCS satisfied § 8.7

fails on the merits, too. The stipulation releases SGM only from claims that were "due and owing" as of the date the provider agreements were transferred to SGM. But DHCS retained the right to assert new claims based on future audits. SGM never approved the stipulation, which was filed with the court before SGM saw it.

In sum, because all Plaintiffs' claims all depend on their satisfaction of §8.7, Plaintiffs' complaint should be dismissed. Because Plaintiffs have not suggested they could amend their claims to overcome their deficiencies, dismissal should be granted with prejudice and without leave to amend.

B. Plaintiffs' Promissory Fraud Claim Fails for Additional Reasons.

1. The Litigation Privilege Bars Plaintiffs' Fraud Claim.

Plaintiffs never dispute that the litigation privilege applies to statements made in connection with a bankruptcy proceeding. *E.g., In re Cedar Funding, Inc.,* 419 B.R. 807, 825 (B.A.P. 9th Cir. 2009) (a "bankruptcy proceeding is a judicial proceeding within the scope of California's litigation privilege."); *Sacramento Brewing Co. v. Desmond, Miller, & Desmond,* 75 Cal.App.4th 1082, 1086 (1999) (holding privilege applied to statement made in a bankruptcy motion). Plaintiffs also do not dispute the substantial breadth of this privilege and the rule that any doubts should be resolved in favor of its application. *See Ramalingam v. Thompson*, 151 Cal.App.4th 491, 500 (2007); *see also Olsen v. Harbison,* 191 Cal.App.4th 325, 333 (2010) ("The breadth of the litigation privilege cannot be understated.") [4]

Instead, Plaintiffs erroneously argue that Defendants are not protected by the litigation privilege because they were not parties to the bankruptcy. The litigation privilege does not apply only to parties; it applies broadly to anyone connected with

[4] Plaintiffs wrongly claim that Defendants "fail to cite a single case applying the litigation privilege to a claim for promissory fraud context." (Opp. at 26.) Not so. Defendants discussed at length *Navarro v. IHOP Properties, Inc.*, which is a claim for promissory fraud resulting from statements made in connection with a bankruptcy proceeding. (*See* Mot. at pp. 14-15, 21.) As here, in that case the plaintiff alleged that the defendant did not intend to comply with its promises in a contract. Of course, this is also not the only case to apply the litigation privilege to claims for promissory fraud. *See, e.g., Billon, Inc. v. Slatin*, 769 F. App'x 443, 444-45 (9th Cir. 2019) (affirming court's dismissal of a claim for promissory fraud based on litigation privilege). Ironically, Plaintiffs did not cite any authority relating to a promissory fraud claim.

the proceedings including witnesses, investigators, jurors. *See Kolar v. Donahue, McIntosh & Hammerton*, 145 Cal.App.4th 1532, 1540 (2006); *see also Olsen*, 191 Cal.App.4th at 334.

Indeed, the Court of Appeal specifically rejected Plaintiffs' argument. In *Olsen*, a plaintiff alleged that an attorney made various fraudulent representations to induce the plaintiff to associate the attorney in as counsel in ongoing litigation. Just as Plaintiffs do here, the plaintiff relied on cases like *LiMandri v. Jenkins* to argue that that the defendant attorney's representations were not privileged because the attorney was "was not a participant in the Klawitter litigation when he made the alleged representations." The Court of Appeal rejected this argument, explaining: "*Although defendant was not actually involved in the Klawitter litigation when his alleged statements were made, these communications were linked to ongoing litigation and his participation was imminent. They therefore fell within the ambit of the litigation privilege*." *Id.* at 335 (emphasis added). As in *Olsen*, SGM's alleged fraudulent representation is privileged because it was made in relation to an ongoing bankruptcy in which its participation in the bankruptcy was, at minimum, imminent. Indeed, SGM's alleged fraudulent representation was also made in preparation for proceedings with the AG and is privileged for that reason as well.

Finally, Plaintiffs argue the litigation privilege does not apply because they allege a tortious course of conduct. This is more nonsense. Plaintiffs' fraud claim is based on SGM's alleged fraudulent representation in the APA that it would pay $610 million to close the transaction. As explained above, this representation is privileged.

2. Plaintiffs' Allegations Do Not Support a Fraud Claim.

Revealingly, Plaintiffs fail to respond to Defendants' detailed argument that their allegations contradict their fraud theory. Instead of countering Defendants' argument, Plaintiffs obfuscate and attempt to summarily dismiss Defendants' argument as just a "semantic ploy." There is no ploy. Rather, as Defendants explained in the motion, Plaintiffs allege that Defendants *never* believed they would have an

obligation to pay $610 million, not that they had an intention of breaching an obligation to pay the $610 million. This distinction is critical. According to Plaintiffs' allegations, Defendants did not commit fraud but just misjudged Plaintiffs' ability to satisfy their conditions. *Richard P. v. Vista Del Mar Child Care Serv.*, 106 Cal.App.3d 860, 865 (1980) ("predictions of future events are ordinarily considered nonactionable expressions of opinion."). Because Plaintiffs allege SGM never thought it would be contractually obligated to pay the $610 million, Plaintiffs cannot establish that Defendants did not intend to comply with such an obligation. There is nothing fraudulent about Defendants having an opinion that Plaintiffs would not be able to satisfy conditions set forth in the contract.

Indeed, Plaintiffs tacitly concede Defendants' point by attempting to modify their theory. They now argue: "the bottom line is that [Defendants] induced Plaintiffs to enter the agreement through the false promise that they [sic] would pay $610 million *if and when* the conditions were satisfied." (Opp. at 28 (emphasis added).) Despite Plaintiffs' attempt to change their story, the theory they pleaded was that Defendants wrongly believed that they would "never" have to pay the $610 million, which is, at best, a non-fraudulent opinion. It is not actionable.

C. Plaintiffs' Claim for Tortious Breach Fails as a Matter of Law.

Defendants cited binding Ninth Circuit authority holding that there is no such claim for "tortious breach of the implied covenant of good faith and fair dealing" in an arms-length transaction such as that at issue here. (Mtn. at 4) citing *Pension Tr. Fund for Operating Eng'rs v. Fed. Ins. Co.*, 307 F.3d 944, 955 (9th Cir. 2002) ("Generally, no cause of action for the tortious breach of the implied covenant of good faith and fair dealing can arise unless the parties are in a special relationship with fiduciary characteristics. Thus, *the implied covenant tort is not available to parties of an ordinary commercial transaction where the parties deal at arms'*

length.") (emphasis added). Plaintiffs have no response to this black-letter law.[5]

Instead, Plaintiffs wrongly state that "numerous courts" have "recognized" a claim for "tortious breach of the implied covenant of good faith and fair dealing" in arms-length transactions. This is false. *Plaintiffs have not cited a single reported case allowing a claim for "tortious breach of the implied covenant of good faith and fair dealing" to survive a motion to dismiss.* There is no such claim under California law.

Plaintiffs' numerous string-cited cases stand only for the unremarkable principle that a plaintiff may allege various *tort* claims (*e.g.* negligence, conversion, etc.) when a contracting defendant has also breached a duty arising *independent* of the contract. *See, e.g. Century of Progress Prods. v. Vivendi S.A.*, 2018 WL 4191340, at *9 (C.D. Cal. Aug. 28, 2018) ("Plaintiffs have alleged Defendants' breach of a duty *not arising from contract*, and resulting harm *distinct from breach*") (emphasis added) (Opp. at fn. 6); *Vestis, LLC v. Caramel Sales, Ltd*. 2019 WL 3312212, at *9 (C.D. Cal. Apr. 30, 2019) (holding that the Plaintiff could seek tort damages for *conversion* despite the existence of a contract) (Opp. at fn. 6); *Robinson Helicopter Co. v. Dana Corp*., 34 Cal.4th 979, 991 (2004) ("We hold the economic loss rule does not bar Robinson's *fraud and intentional misrepresentation claims* because they were independent of Dana's breach of contract.") (emphasis added). Indeed, one of Plaintiffs' cases is the seminal California Supreme Court case *rejecting* a plaintiff's attempt to tortify a breach of contract. In *Erlich v. Menezes*, the California Supreme Court rejected a plaintiff's attempt to bring a claim for "negligent breach of contract" and in so doing stated: "conduct amounting to a breach of contract becomes tortious only when it also violates a duty independent of the contract arising from principles of tort law. … An omission to perform a contract obligation is never a tort, unless that omission is also an omission of a legal duty." 21 Cal.4th 543, 551 (1999) (citation

[5] Instead, they seek to "distinguish" the cases by noting they discuss special/fiduciary relationships. That is precisely the point. The claim, if it exists at all, exists ***only*** in such cases. This is not one of those cases.

omitted). Plaintiffs' cases do not support their made up cause of action. [6]

Defendants' motion also demonstrated that Plaintiffs' "tortious breach" claim must be dismissed because it is duplicative of their failed breach of contract and fraud claims. (Mtn. at 10.) Plaintiffs counter by summarily concluding that argument is "demonstrably false" without attempting to demonstrate as much. (Opp. at 28 n.7.) Plaintiffs likely do not attempt a defense of this argument because they concede it. Elsewhere in their Opposition, Plaintiffs state "Plaintiffs' third claim for relief alleges Tortious Breach of Contract (Breach of the Implied Covenant of Good Faith and Fair Dealing) based on the same allegations supporting the first claim, for breach of contract." (Opp. at 29:10-12); *id.* ("The third claim for relief is based on the same conduct at issue in the breach of contract claim….").[7]

Knowing that their cases do not support their claim and having conceded its

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[6] All of Plaintiffs' cases are inapposite. *See Najor v. Wells Fargo Bank, N.A*. 2019 WL 1858502, at *4-5 (S.D. Cal. Apr. 25, 2019) (no "tortious breach of the implied covenant claim." Plaintiff pled a *fraud* claim and, separately, a standard claim for breach of the implied covenant); *Dairy v. Harry Shelton Livestock*, 2019 WL 631493, at *10 (N.D. Cal. Feb. 14, 2019) (Holding only that Plaintiff's *negligence* and *fraud* claims should not be dismissed under the economic loss rule.); *Expedited Packages, LLC v. Beavex Inc.*, 2015 WL 13357436, at *3 (C.D. Cal. Sept. 10, 2015) (conversion claim not barred) (Opp. at fn. 6) *Kanter v. Playbill, Inc*., 2017 WL 10591601, at *7 (C.D. Cal. Aug. 31, 2017) (holding only that the economic loss rule did not bar plaintiff's fraud claim); *Bullard v. Wastequip, Inc*., 2014 WL 10987394, at *8 (C.D. Cal. Sept. 11, 2014) (dismissing claim for promissory fraud); *Foley v. Aintabi*, 2013 WL 12130015, at *6 (C.D. Cal. Nov. 6, 2013) (fraud claims not barred by the economic loss rule); *Fortune Mfg. Co. v. Zurn Indus., LLC*, 2011 WL 13218043, at *3 (C.D. Cal. Aug. 31, 2011) (claim for intentional interference with contractual relations); *Unique Functional Prod., Inc. v. JCA Corp.*, 2011 WL 13355975, at *6 (S.D. Cal. May 4, 2011) (fraud claim not barred by economic loss rule); *Gentec Enterprises Inc v. Transistor Devices Inc*, 2011 WL 13217566, at *3 (C.D. Cal. Jan. 31, 2011) (same); *Velocity Staffing Corp., Inc. v. Resolve Staffing, Inc.*, 2008 WL 11342746, at *3 (C.D. Cal. June 16, 2008) (same)*; Rejects Skate Magazine, Inc. v. Acutrack, Inc*., 2006 WL 2458759, at *5 (N.D. Cal. Aug. 22, 2006)(discussing the personal injury or property damage exception to the economic loss rule); *StreamCast Networks, Inc. v. IBIS LLC*, 2006 WL 5720345, at *10 (C.D. Cal. May 2, 2006) (fraud claim); *El Dorado Irrigation Dist. v. Traylor Bros*., 2006 WL 306914, at *5 (E.D. Cal. Feb. 7, 2006) (personal injury not required for fraud); *Putnam v. Putnam Lovell Grp. NBF Sec., Inc*., a Delaware corporation, 2005 WL 2463951, at *9 (N.D. Cal. Oct. 5, 2005) (fraudulent inducement). Plaintiffs' only case even discussing a claim for tortious breach of the implied covenant is *Bea v. Sw. Airlines Co*., No. 2005 WL 646074, at *4 (N.D. Cal. Mar. 17, 2005), a fifteen year old, unpublished decision that misapplied the economic loss rule, was wrongly decided, and has never been cited for that proposition.

[7] As stated in Defendants' moving papers, to the extent that it is different from the breach of contract claim, it would be barred by the litigation privilege also. (Mtn. at 25-26.)

redundancy, Plaintiffs finally attempt to misdirect this Court with case law stating the well-known principle that every contract contains an implied covenant of good faith and fair dealing. (Opp. at 27:11-28.) That is true. But Plaintiffs did not plead breach of the implied covenant of good faith and fair dealing; they pled *tortious* breach of contract and seek punitive damages. No such claim exists in arms-length transactions such as this and Plaintiffs' made-up claim must be stricken.

D. Plaintiffs Cannot Establish Alter-Ego Liability.

1. Plaintiffs Knew of the Non-SGM Defendants' Existence and Chose Not to Contract With Them.

Defendants cited multiple cases explaining that a plaintiff cannot invoke the alter-ego doctrine when the plaintiff had knowledge of the existence of the alleged alter-egos but nevertheless decided to contract solely with the defendants instead of or in addition to the principal. *See, e.g., Lynch v. McDonald*, 155 Cal. 704 (1909). In response, Plaintiffs cite two cases, *G. E. J. Corp. v. Uranium Aire, Inc.* and *Hiehle v. Torrance Millworks*, which they contend contradict Defendants' arguments. Not so.

Plaintiffs first misplace their reliance on *G. E. J. Corp. v. Uranium Aire, Inc.* That case involved a principal entity that assured the plaintiff that while it will not sign a contract, it "*would be responsible for* [its subsidiary corporation's] *obligations contained in the* [contract] *and would stand behind* [its subsidiary corporation] *in the performance of the option agreement*." *G. E. J. Corp. v. Uranium Aire, Inc.*, 311 F.2d 749, n.6 (9th Cir. 1962) (emphasis added). The court held that injustice would result if the subsidiary's corporate existence was maintained because the principal entity represented that it would be responsible for its subsidiary's obligations and would stand behind its subsidiary in performance of the contract. *Id*. at 757.

Hiehle v. Torrance Millworks also fails to support Plaintiffs' cause. In that case, the principals of a corporation made multiple misrepresentations regarding the corporation's financial condition to a corporate employee to entice the employee to lend money to the corporation. 126 Cal. App. 2d 624, 625-26 (1954). The principal

also represented that he would pay the interest on the loan. *Id*. at 630. After the corporation filed for bankruptcy, the plaintiff filed a complaint in intervention arguing that the corporation was the principals' alter ego. *Id*. at 627. The court concluded that the principals were estopped from denying their representations regarding the status of the corporation's finances. *Id*. at 630.

Unlike the cases they rely on, Plaintiffs have not and cannot allege that any of the Non-SGM Defendants represented they would be responsible for SGM's contractual obligations. Indeed, the parties specifically negotiated the strict terms of *SGM*'s potential liability. Inequitably, Plaintiffs are attempting to circumvent their negotiated relationship through manufactured tort claims and claims for alter-ego.

Knowing its case law is unsound, Plaintiffs next attempt to remedy the gaping holes in their alter-ego claim by conflating the elements of alter ego. Specifically Plaintiffs argue that alter ego liability is appropriate because the Non-SGM Defendants allegedly "repeatedly stated that SGM is the acquisition arm of KPC, but that KPC and SGM are one and the same business entity led by Chaudhuri" (Opp. at 33:5-8). But Plaintiffs' allegation does not have any bearing on the issue at hand. Plaintiffs' allegations, at best, would only relate to the unity of ownership prong of the alter ego claim, not the injustice prong that serves as the basis for Defendants' motion. Plaintiffs' allegations do not establish that any Non-SGM Defendant agreed to guarantee SGM's liabilities. Because they had full knowledge of the Non-SGM Defendants' identity and affirmatively chose to contract solely with SGM, Plaintiffs cannot satisfy the injustice prong of alter ego liability as a matter of law. [8]

2. Plaintiffs' Allegations Compel Dismissal of KPC Healthcare.

In their motion, Defendants demonstrated that Plaintiffs' Complaint *itself* alleges that KPC Healthcare has been sold to an Employee Stock Ownership Plan

[8] Plaintiffs now claim they did not know the relationship between SGM and the Non-SGM Defendants. (Opp. at n. 12). Plaintiffs' own Complaint proves otherwise and shows that they undertook substantial due diligence involving numerous advisors and attorneys for the $610,000,000 deal. Compl. ¶ 40-44.

that is not owned by Dr. Chaudhuri or SGM and therefore cannot be SGM's alter ego. (*See* Compl. ¶ 41.) In opposition, Plaintiffs argue that referencing SGM's offer in paragraph 41 of their Complaint, does not constitute a concession that KPC Healthcare, Inc. is not an alter ego for any of the other defendants. Opp. at p. 33:3-6. Plaintiffs are wrong. Contradictions between the contents of a document referenced in the complaint and the allegations in the complaint may defeat Plaintiffs' claim. *See Nishimatsu Const. Co. v. Houston Nat. Bank*, 515 F.2d 1200, 1206–07 (5th Cir. 1975) (plaintiff failed to state a claim against the defendant when an agreement that was incorporated into the complaint contradicted the allegations in the complaint).

Paragraph 41 of Plaintiffs' complaint incorporates parts of SGM's offer, dated August 13, 2018. In SGM's offer, it states that KPC Healthcare Inc. has been sold to an Employee Stock Ownership Plan, which operates for the benefit of the employees. Compl. ¶ 41. This is wholly inconsistent with Plaintiffs' allegation that Dr. Chaudhuri is the majority (or sole) shareholder of KPC Healthcare, Inc. Compl. ¶ 15. It is evident that KPC Healthcare Inc. is not owned by SGM or any other defendant and cannot be SGM's alter ego. KPC Healthcare Inc. should also be dismissed for this reason.

It is not surprising that Plaintiffs' alter ego allegations are flatly contradicted by documents. As set forth in Defendants' motion, Plaintiffs' alter ego allegations must be dismissed because they offer no specific facts – only conclusory allegations consisting of a boilerplate recitation of the alter ego factors pled solely on "information and belief." That alone requires dismissal of the Non-SGM defendants.

IV. CONCLUSION

For the reasons discussed in its Moving papers and above, Defendants request that the Court dismiss each claim asserted by Plaintiffs.

Dated: March 11, 2020

BARNES & THORNBURG LLP

By:/s/Kevin D. Rising
Kevin D. Rising
Counsel for Defendants