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UNITED STATES BANKRUPTCY COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA -
LOS ANGELES 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 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 ASC, LLC

Debtors and Debtors In Possession.

Lead Bankruptcy Case No. 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
CASE NO.: 2:18-bk-20179-ER
CASE NO.: 2:18-bk-20180-ER
CASE NO.: 2:18-bk-20181-ER

Chapter 11 Cases
Hon. Judge Ernest M. Robles

Adversary No. 2:20-ap-01001-ER

PLAINTIFFS' OPPOSITION TO DEFENDANTS' SPECIAL MOTION TO STRIKE PURSUANT TO CALIFORNIA CODE OF CIVIL PROCEDURE SECTION 425.16

Hearing Date and Time:
Date: March 18, 2020
Time: 9:30 a.m.
Place: Courtroom 1568
255 E. Temple St.
Los Angeles, CA 90012

1820151200305000000000003

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.

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Plaintiffs Verity Health System of California, Inc. ("VHS"), St. Vincent Medical Center and its wholly-owned subsidiary (collectively, "St. Vincent"), St. Vincent Dialysis Center, Inc., St. Francis Medical Center ("St. Francis"), Seton Medical Center ("Seton," and together with St Francis and St. Vincent, the "Plaintiff Hospitals" or the "Hospitals"), and Verity Holdings, LLC ("Verity Holdings"), and the above-captioned debtors and debtors in possession (collectively, the "Debtors" or "Plaintiffs"), submit this opposition (the "Opposition") to the *Special Motion to Strike Pursuant to Section 425.16 of the California Code of Civil Procedure* [Adv. Docket No. 39][1] (the "Motion"), filed by Defendants Kali P. Chaudhuri, M.D., Strategic Global Management, Inc., KPC Healthcare Holdings, Inc., KPC Health Plan Holdings, Inc., KPC Healthcare, Inc., and KPC Global Management, LLC (collectively, "Defendants").

I. INTRODUCTION

In its Special Motion to Strike the Complaint, pursuant to California Code of Civil Procedure section 425.16 (the "anti-SLAPP" statute), Defendants advance the stunning position that *every* commercial transaction involving a Chapter 11 debtor involves free speech and protected petitioning activity merely because of the debtor's bankrupt status. Worse, Defendants ask this Court to rule that there can be no liability as a matter of law for committing fraud against a debtor, again simply because of their status in bankruptcy and the public nature of the proceeding. Defendants' position is patently spurious, lacking in legal support, and offensive to public policy.

The Defendants filed their anti-SLAPP motion in order to stall the debtors' Adversary Proceeding for years while they seek interlocutory review of any adverse ruling.[2] But their strategy will fail because the anti-SLAPP statute does not apply to the Adversary Proceeding, which is premised on federal question jurisdiction. Further, this case falls within a statutory commercial

[1] As used herein, "Adv. Docket No." refers to the docket of the instant adversary proceeding, Adv. Case No. 2:20-ap-01001-ER (the "Adversary Proceeding"), and "Docket No." refers to the docket of the above-captioned, jointly administered bankruptcy cases, Lead Case No. 2:18-bk-20151-ER (the "Cases").

[2] Indeed most, if not all, of the issues raised in the Motion are more appropriately resolved in the context of a motion to dismiss—which Defendants filed simultaneously with the Motion. What looks to be Defendants' primary issue—namely, Plaintiffs' satisfaction of section 8.7 of the APA—is the same in both motions. The Motion is needlessly duplicative of the motion to dismiss and simply increases costs and complexity without any real value to resolving the underlying complaint.

activity exception to the anti-SLAPP statute, which makes any order denying their motion immune from interlocutory review. The commercial speech exception set forth in Code of Civil Procedure section 425.17 applies and Defendants' motion should be denied. This case should proceed on its merits.

Fortunately, the Complaint does not fall within the ambit of the anti-SLAPP statute. The "principal thrust or gravamen" of the Complaint is not protected petitioning activity, but rather a wrongful course of conduct by Strategic Global Management, Inc. ("SGM") and its alter egos designed to lock Plaintiffs into that certain asset purchase agreement ("APA") for the sale of four hospitals, with which Defendants had no intention of complying. *See* Complaint for Breach of Contract, Promissory Fraud, and Tortious Breach of Contract (Breach of Implied Covenant of Good Faith and Fair Dealing) ("Compl.") [Adv. Docket No. 1.] As a matter of law, such wrongful commercial conduct is not protected by the anti-SLAPP statute. Plaintiffs' status as debtors in bankruptcy cases does not change that fact. Accordingly, Defendants' Special Motion to Strike should be denied because they have not carried their burden of demonstrating that the "principal thrust or gravamen" of the Complaint involves protected petitioning activity.

Even if Defendants had met their burden under the first prong of the anti-SLAPP statute (they have not), Plaintiffs are likely to prevail on the merits, as set forth below. The three claims for relief asserted in the Complaint are well grounded in California law and the Bankruptcy Code and supported by detailed factual allegations. Contrary to Defendants' meritless assertions, they are not "privileged" to defraud Plaintiffs and violate the APA simply because the estate is in bankruptcy. The Motion should be denied.

II. BACKGROUND FACTS

A. General Background

1. On August 31, 2018, (the "Petition Date"), the Debtors each filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code (the "Cases"). The Cases are currently jointly administered before the Court. [Docket No. 17]. Since the Petition Date, the Debtors have been operating their businesses as debtors in possession pursuant to §§ 1107 and 1108.

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2. On August 13, 2018, the Debtors received an offer letter from SGM on letterhead that included the KPC logo, offering to purchase the Hospitals from SGM for $610 million (the "Purchase Price"). The offer letter made various representations about SGM and its affiliates and their expertise in the provision of managed health care services. The Debtors selected SGM to be the stalking-horse bidder based on its offer to acquire the Hospitals that consisted of a cash payment in the amount $610,000,000, plus assumption of certain liabilities, and payment of cure costs associated with any assumed leases, contracts and assumption of other obligations. *See* APA, Section 1.1. The Debtors selected SGM in reliance on Defendants' representations and inducements. *See* Request for Judicial Notice In Support of Opposition to Defendants' Motion to Dismiss and Opposition to Defendants' Special Motion to Strike ("RJN"), Exhibit GG (Compl., ¶¶ 40, 41, 42).

3. On January 8, 2019, SGM executed the APA to acquire the Plaintiff Hospitals and related assets for the Purchase Price. *See* RJN, Ex. GG (Compl., ¶ 44). As discussed further below, it contains provisions requiring approval by the Bankruptcy Court, approval by the Attorney General, and transfer Medicare and Medi-Cal provider agreements to SGM. *See* RJN, Ex. GG (Compl., ¶ 46, Ex. A).

4. On January 17, 2019, the Debtors filed a motion [Docket No. 1279] (RJN, Ex. A, the "Sale and Bidding Procedures Motion") to approve, among other things, the form of an asset purchase agreement with SGM and related "stalking horse" protections and bidding procedures for the sale of the Hospitals [Sale and Bidding Procedures Mot. at 1], which the Court approved [Docket No. 1572] (RJN, Ex. B, the "Bidding Procedures Order"). SGM served as the stalking-horse bidder (the "Stalking-Horse Bidder") under the terms of the Bidding Procedures Order. *See* RJN, Ex. B, Bidding Procedures Order at 7.

5. The Bidding Procedures Order incorporated and approved a revised Section 8.6 in the asset purchase agreement (the "APA") [Docket 1572, Docket 2306]. *See* RJN, Ex. B and Ex. E. Specifically, the parties heavily negotiated a provision in the amended APA addressing the California Attorney General's (the "Attorney General") right to review and approve the proposed sale and the Debtors right to obtain a supplemental sale order in furtherance of a sale closing. On

May 17, 2019, Chaudhuri filed an Early Termination Notice with the Federal Trade Commission regarding the SGM Sale. The filing lists the "Acquiring Party" as "Kali P. Chaudhuri, trustee," and the "Acquired Party" as "Verity Health System of California, Inc." RJN, Ex. GG (Compl., ¶ 55). Defendants thereafter described the SGM Sale on their websites as an acquisition by KPC and Chaudhuri. RJN, Ex. GG (Compl., ¶¶ 56-57).

6. Defendants thereafter described the SGM Sale on their websites as an acquisition by KPC and Chaudhuri. *See* RJN, Ex. GG (Compl., ¶¶ 56-57).

C. Attorney General Review and the AG Conditions Motion

7. One of the conditions to closing under the APA was (i) the approval by the Attorney General Of California (the "Attorney General"), pursuant to California Corporations Code § 5914 and title 11 of the California Code of Regulations, § 999.5, and (ii) that the Attorney General did not impose any conditions that were "materially different" that those set forth in Schedule 8.6 to the APA. Under Section 8.6 of the APA, the APA also provided that SGM "shall reasonably cooperate in any efforts to render the Supplemental Sale Order a final, non-appealable order." *See* RJN, Ex. GG (Compl., ¶ 63).

8. During the week of August 26, 2019, Deputy Attorney General Scott Chan held public hearings at each of the Hospitals to solicit comments regarding the SGM Sale. At those public meetings, Peter Baronoff, as CEO and a representative of Defendants, made public statements to the effect that SGM is the acquisition arm of KPC, but that KPC and SGM are one and the same business entity led by Chaudhuri. *See* RJN, Ex. GG (Compl., ¶ 66).

9. On September 25, 2019, the Attorney General consented to the sale subject to certain conditions (the "2019 Conditions"). The 2019 Conditions contained numerous conditions (the "Additional Conditions") that were materially different than those SGM contractually agreed to in Schedule 8.6. SGM's Chief Executive Officer confirmed that SGM would not close the sale if the Additional Conditions remained extant. *See* RJN, Ex. F, Docket No. 3188.

10. On September 30, 2019, the Debtors filed a motion [Docket No. 3188] (the "AG Conditions Motion"), which sought (i) entry of an order enforcing the Sale Order, (ii) a finding that the sale was free and clear of certain additional conditions imposed by the Attorney General, and

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(iii) a finding limiting the sale to only those conditions to which SGM contractually agreed to assume in Schedule 8.6 of the APA. *See* RJN, Ex. F. On October 10, 2019, SGM filed a statement in support of the AG Conditions Motion [Docket No. 3356] requesting that the Court enter an order granting the AG Conditions Motion. *See* RJN, Ex. G. On October 23, 2019, the Court entered a memorandum of decision (the "AG Conditions Memorandum Decision") [Docket No. 3446] setting forth the Court's ruling to grant the AG Conditions Motion and requesting that the Debtors lodge an order consistent with the ruling. *See* RJN, Ex. H.

D. The AG Conditions Order

11. After entry of the AG Conditions Memorandum Decision, the Attorney General, the Debtors, and SGM engaged in discussions amongst each other concerning a proposed form of order. *See* RJN, Ex. I, Docket No. 3573 at 3. Over a ten day period, the Debtors and the Attorney General attempted to satisfy SGM's concerns with respect to the wording of the proposed order granting the AG Conditions Motion (the "Proposed Order"). *See id.* Despite their efforts, the Debtors were unable to secure SGM's joinder in the Stipulation; however, after careful consideration, the Debtors and the Consultation Parties under the Bidding Procedures Order determined that entry of the Proposed Order was in the best interests of the estates given that it ensured that the Attorney General would not appeal the Proposed Order and it contained the exact required findings under Section 8.6 of the APA. *See id.*

12. On November 8, 2019, the Debtors and the Attorney General filed a stipulation [Docket No. 3572] (the "Stipulation") and lodged a proposed order granting the AG Conditions Motion [Docket No. 3574] (the "Proposed Order"). *See* RJN, Exs. J and K. Pursuant to the Stipulation, (i) the Attorney General agreed to the Proposed Order authorizing the sale free and clear of "Additional Conditions," (ii) the Debtors agreed to obtain a withdrawal of the Memorandum Decision, and (iii) the Attorney General agreed not to appeal the Proposed Order. *See* Stipulation at 3. The Proposed Order adopted the language required by Section 8.6 of the APA nearly verbatim. RJN, Ex. K, Proposed Order at 3; APA § 8.6 at 33.

13. On November 11, 2019, SGM filed an objection [Docket No. 3582] to the Proposed Order and lodged a competing order [Docket No. 3583]. *See* RJN, Exs. L and M. SGM's objection

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sought revisions to the Proposed Order to rectify purported ambiguities "that may actually result in litigation between the AG and SGM." RJN, Ex. L, Docket No. 3582 at 4. The proposed revisions went beyond the relief the Debtors were required to obtain pursuant to Section 8.6 of the APA.

14. On November 13, 2019, the Court held a hearing on the Stipulation, at which the Court overruled SGM's objection to the Proposed Order. On November 14, 2019, the Court entered the Proposed Order, as modified on the record at the November 13 hearing, granting the AG Conditions Motion [Docket No. 3611] (the "AG Conditions Order"). *See* RJN, Ex. N.

15. On November 29, 2019, despite the modifications to the Proposed Order, SGM filed a notice of appeal [Docket No. 3726] related to the AG Conditions Order. *See* RJN, Ex. P.

E. Transfer Of The Medicare And Medi-Cal Provider Agreements

16. As noted above, the APA also required that Plaintiffs secure the transfer of Medicare and Medi-Cal Provider Agreements to SGM. On November 19, 2019, Plaintiffs obtained a settlement with the Centers for Medicare and Medicaid Services, an agency of the United States Department of Health & Human Services, providing for the transfer of their Medicare Provider Agreements to SGM without successor liability, thereby satisfying their remaining obligations under Article 8.7 of the APA. [Docket No. 3680.] *See* RJN, Ex. O.

17. With respect to California Department of Health Care Services ("DHCS"), Plaintiffs secured an Order [Docket No. 3372] from the Bankruptcy Court authorizing the transfer free and clear of any interests asserted by DHCS, in addition to the Sale Order which terminated any creditor's recoupment rights [Docket No. 2306]. *See* RJN, Exs. Q and E. Those Orders afforded equal or greater protection to SGM than any settlement could have, thereby satisfying Section 8.7. SGM disagreed that the DHCS Order and the Sale Order satisfied Section 8.7. Consequently, although not necessary but given SGM's position, on November 22, 2019, Plaintiffs reached a settlement agreement with DHCS, which the Bankruptcy Court approved. [Docket Nos. 3786 & 3787.] *See* RJN, Exs. R and S.

E. The Scheduling Order

18. On November 15, 2019, the Debtors filed a motion [Docket No. 3621] to continue deadlines related to a motion to approve the Debtors' disclosure statement [Docket No. 2995]. *See*

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RJN, Exs. T and U. In the motion, the Debtors requested the continuance based on "formal correspondence material to the sale transaction" that the Debtors anticipated receiving from SGM. *See* RJN, Ex. T, Docket No. 3621 at 2.

19. On November 18, 2019, the Court entered an order on the Debtors' request to continue the disclosure statement deadlines [Docket No. 3633] (the "Scheduling Order"). *See* RJN, Ex. V. The Scheduling Order granted the Debtors' request to continue the deadlines and further provided that SGM was obligated to promptly close the sale under Section 8.6 of the APA. The Scheduling Order provides, in relevant part, that:

> The Debtors have complied with their obligation under the APA to obtain a final, non-appealable Supplemental Sale Order. Consequently, SGM is now obligated to promptly close the SGM Sale, provided that all other conditions to closing have been satisfied.

See RJN, Ex. V., Sched. Order at 2. With respect to Section 8.7 of the APA, the Court concluded: "[t]he Debtors materially complied with Article 8.7 by obtaining an order authorizing the transfer of the Medi-Cal Provider Agreements free and clear of any interest asserted by the DHCS" and that "Debtors obtained a settlement with the Centers for Medicare and Medicaid Services providing for the transfer of their Medicare Provider Agreements to SGM, thereby satisfying their remaining obligations under Article 8.7 of the APA." RJN, Ex. AA, Docket 3723 at 7.

20. In conjunction with the Scheduling Order, the Court issued a memorandum of decision [Docket No. 3632] (the "Scheduling Memorandum Decision"). *See* RJN, Ex. X. The Court further set forth findings and conclusions concerning Section 8.6 of the APA "[t]o facilitate an expeditious and successful resolution of these cases." RJN, Ex. X, Sched. Mem. Decision at 2.

21. On November 29, 2019, SGM appealed the Scheduling Order. *See* RJN, Ex. W, Docket No. 3727. The appeals of the AG Conditions Order and Scheduling Order were an unexpected maneuver by SGM. As noted, above, SGM had participated in the carefully negotiated revisions to Section 8.6 of the APA, and the inclusion of the "Evaluation Period" therein, "to prevent it from being required to close the sale if there was a risk that the Supplemental Sale Order could be overturned on appeal." *See* RJN, Ex. X, Sched. Mem. Decision at 4. Indeed, SGM committed in Section 8.6 to help the Debtors avoid any appeal by "reasonably cooperat[ing] in any

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efforts to render the Supplemental Sale Order a final, non-appealable order." *See* RJN, Ex. C, APA § 8.6 at 33. The Debtors did not anticipate that SGM would treat Section 8.6 of the APA or the Evaluation Period or the cooperation promise as creating an illusory closing condition to be frustrated at SGM's discretion by the simple expedient of the filing of its own notice of appeal.

F. The MAE Order

22. On November 26, 2019, the Court held a status conference (the "Status Conference") in light of mounting uncertainties surrounding SGM's intention to close the sale. At the Status Conference, the Court interpreted the "Material Adverse Effect" provisions of the APA, found that the Debtors had satisfied all conditions to closing because no Material Adverse Effects had occurred, and surmised, "I suspect that this [Sale] will close and if not, then [SGM] will pay damages pursuant to this agreement." RJN, Ex. Y, Nov. 26, 2019 Hr'g Tr. at 14.

23. On November 27, 2019, the Bankruptcy Court entered an order [Docket No. 3724] (RJN, Ex. Z, the "MAE Order" and, together with the AG Conditions Order and the Scheduling Order, the "Orders") and memorandum of decision [Docket No. 3723] (RJN, Ex. AA, the "MAE Memorandum Decision") finding SGM was obligated to close the sale by no later than December 5, 2019. Specifically, the Court found that (i) Section 9.1(c) of the APA authorized the Court to exclusively determine Material Adverse Effect issues without the right of appeal and (ii) no Material Adverse Effects had occurred under the APA. *See* RJN, Ex. AA, MAE Mem. Dec. at 4, 6. As a result, "SGM would not be excused from closing the sale under Article 8.4 of the APA." *Id.* at 6.

24. On December 3, 2019, SGM appealed the MAE Order. *See* RJN, Ex. BB, Docket No. 3746.

G. Termination of the APA

25. SGM did not close the sale on December 5, 2019. On December 6, 2019, the Debtors filed an emergency motion [Docket No. 3773] for issuance order to show cause why SGM failed to close the sale by December 5, 2019. *See* RJN, Ex. CC. On December 9, 2019, the Court entered an order [Docket No. 3784] denying the emergency motion and providing that "[a]ny efforts undertaken by the Debtors with respect to the alternative disposition of the Hospitals" would

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not violate the APA. RJN, Ex. DD, Docket No. 3784 at 2. In the accompanying memorandum of decision [Docket No. 3783], the Court recognized that:

> By failing to close, SGM risks the loss of its $30 million good-faith deposit as well as the possibility of damages for breach of contract in an amount of up to $60 million. . . . In the future, the Debtors will have an opportunity to litigate the issues of whether SGM has breached the APA and whether the Debtors are entitled to retain SGM's good-faith deposit.

RJN, Ex. EE, Docket No. 3783 at 2 (emphasis added). On December 27, 2019, the APA terminated as a result of SGM's failure to close the sale. *See* RJN, Ex. FF, Docket No. 3899.

H. The Adversary Proceeding Against SGM and Its Alter Egos

26. On January 3, 2020, the Debtors filed the Complaint against SGM and its alter egos, which commenced the Adversary Proceeding. *See* RJN, Ex. GG, Adv. Docket No. 1. The Complaint asserts claims arising from SGM's conduct with respect to the APA and the SGM Sale, including breach of contract, promissory fraud, and tortious breach of contract based on SGM's and the other defendants' breaches of the implied covenant of good faith and fair dealing.

27. The Court has set the Adversary Proceeding for trial during the week of November 30, 2020, and has required all dispositive motions be heard not later than October 27, 2020. *See* RJN, Ex. HH, Adv. Docket No. 4.

28. SGM filed a motion to stay the Adversary Proceeding (the "Stay Motion") based on its claim that the Court does not have jurisdiction to address the issues raised in the Complaint while the Appeals are pending. *See* RJN, Ex. II, Docket No. 19. By Order dated February 14, 2020, the Court denied that motion (the "Order Denying Stay"). *See* RJN, Ex. JJ, Docket No. 35. The Defendants filed this Motion on February 19, 2020.

III. ARGUMENT

Recognizing the "disturbing abuse of Section 425.16, the California Anti-SLAPP Law, which has undermined the exercise of the constitutional rights of freedom of speech and petition for the redress of grievances," the California Legislature enacted several exceptions to the anti-SLAPP statute in 2003, including the "commercial exemption." If the court denies a special motion to strike based on one of those exemptions, then "the appeal provisions in [the anti-SLAPP statute]

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do not apply to that action," and the ruling is not subject to interlocutory review. Cal. Civ. Proc. Code § 425.17(e).

If no statutory exception applies, then a two-part test is used to determine if a cause of action should be stricken under the anti-SLAPP statute. First, the defendant bears the initial burden to show the plaintiff's claims arise "from any act of [the defendant] in furtherance of [its] right of petition or free speech under the United States or California Constitution in connection with a public issue[.]" Cal. Civ. Proc. Code § 425.16(b)(1); *Chavez v. Mendoza*, 94 Cal. App. 4th 1083, 1087 (2001). Second, after the court determines protected free speech or petition is at issue, the burden shifts to the plaintiff to establish a reasonable probability it will prevail on its claims. *Chavez*, 94 Cal. App. 4th at 1087.

Here, the Complaint centers on a commercial dispute, the wrongful failure of the proposed purchase and sale of four operating hospitals providing patient care services with related inventories of drugs and other hospital supplies to Defendants who themselves directly or indirectly provide patient care services. It does not center on Defendants' activities petitioning the Bankruptcy Court for relief, except for approval of Defendants' proposed expansion of activities as a for profit supplier of hospital patient care services. To the extent the case involves direct speech, i.e., written or oral representations to the Debtors upon which Defendants desired the Bankruptcy Court to rely as supervisor of an out of the ordinary course commercial transaction, it is commercial speech relating to Defendants' purported desire to expand its own for profit operations or services. As such, the "speech," falls within the exceptions to the anti-SLAPP statute. Further, Defendants have not satisfied (and cannot satisfy) their initial burden of demonstrating that Verity's Complaint arises out of activity protected by the anti-SLAPP statute. Finally, Verity can plainly demonstrate a likelihood of prevailing on the merits. Accordingly, the motion should be denied.

A. <u>The Anti-SLAPP Statute Does Not Apply to the Adversary Proceeding</u>

There is little question that California's anti-SLAPP statute does not apply to lawsuits, such as the Adversary Proceeding, that are premised on federal question jurisdiction. *Hilton v. Hallmark Card Inc.,* 599 F.3d 894, 901 (9th Cir. 2010) (federal courts have no jurisdiction to consider California anti-SLAPP claims posed against a plaintiff's federal Lanham Act claims); *Bulletin*

Displays, LLC v Regency Outdoor Advert., Inc., 448 F. Supp. 2d 1172, 1180-1181 (C.D. Cal. 2006) (California anti-SLAPP statute not applicable to federal RICO and Clayton Act *federal question claims).* The anti-SLAPP statute "does not apply to federal question claims in federal court because such application would frustrate substantive federal rights." *Id.* at 1180; *see also Globetrotter Software, Inc. v Elan Computer Group, Inc.,* 63 F. Supp. 2d 1127, 1130 (N.D. Cal. 1999) (anti-SLAPP statute is not applicable to federal claims); *In re Bah,* 321 B.R. 41, 46 (9th Cir. B.A.P. 2005) ("'We [. . .] agree with the *Globetrotter* court that the anti-SLAPP statute may not be applied to matters involving federal questions.").

There is also little question that this Court has core subject matter jurisdiction over all of the claims raised in the Complaint pursuant to 28 U.S.C. § 157(b)(2), both as a matter of law and by agreement of the parties. *See* RJN, Ex. GG (Compl. ¶¶ 1-3) . Beyond a general footnote reservation of rights,[3] the Motion does not challenge the Court's subject matter jurisdiction under 28 U.S.C. § 157(b)(2), to hear all matters related to the Complaint. Nor does the Motion challenge the existence of contractual consent.[4] Further, core jurisdiction under the Bankruptcy Code is unquestionably a form of federal question jurisdiction, as it derives from federal statutes. *See, e.g.*, *Penson Techs. LLC v. Schonfeld Grp. Holdings LLC (In re Penson Worldwide, Inc, LLC)* 587 B.R. 6 (Bankr. D. Del. 2018) (discussing generally bankruptcy court jurisdiction as a subset of federal question jurisdiction); *Bavelis v. Doukas (In re Bavelis*), 453 B.R. 832 (Bankr. S.D. Ohio 2011) (national wide service of process with respect core bankruptcy claims permitted under federal question jurisdiction rendering minimum contacts analysis irrelevant) (citations omitted); *Erhlich v. American Express Travel Related Servs. Co. (In re Guilmette),* 202 B.R. 9, 12 (Bankr. N.D. 1996) ("The 'arising under' basis involves federal question jurisdiction and any 'arising under'

[3] *See* Mot. at n.1.

[4] In their motion to dismiss the complaint [Adv. Docket No. 40], Defendants rely on prepetition contract dispute cases to assert this Court lacks core subject matter jurisdiction over claims that arise exclusively from post-petition conduct of Defendants relating to the purchase and sale of assets subject this Court's jurisdiction as property of the estate. *Compare In re E. Orange Gen. Hosp., Inc.*, 587 B.R. 53, 73 (D.N.J. 2018) ("The Bankruptcy Court possessed jurisdiction over proceedings to enforce the Sale Order; indeed, the motion to enforce the Sale Order was a 'core' proceeding.") *with Security Farms v. Int'l Bhd. of Teamsters, Chauffers, Warehousemen & Helpers,* 124 F.3d 999, 1008 (9th Cir. 1997) ("Actions that do not depend on bankruptcy laws for their existence and that could proceed in another court are considered 'non-core.'").

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proceeding is based on a substantive claim under title 11.") (citations omitted). This logic, that the anti-SLAPP statute is not applicable to federal question claims, follows cleanly from Congressional extension of authority to the Bankruptcy Courts to consider claims directly impacting the estate under § 157(b)(2), which, in turn, is derived from the exclusive subject matter under 28 U.S.C. § 1334(a), (e)(1) granted to the District Courts for cases under Title 11 and property of the Debtor and property of the estate.[5] The Motion should be denied because the Adversary Proceeding implicates federal question jurisdiction.

B. The Complaint Falls Within The Commercial Exemption To The Anti-SLAPP Statute, Code Civ. Proc. § 425.17

Concerned with the "disturbing abuse" of the anti-SLAPP statute, the California Legislature enacted Code of Civil Procedure section 425.17 in 2003 to exempt certain speech from the anti-SLAPP statute. Section 425.17(c) sets forth the "commercial speech" exemption to anti-SLAPP, which courts interpret as exempting from the anti-SLAPP statute a cause of action arising from commercial speech when:

> (1) the cause of action is against a person primarily engaged in the business of selling or leasing goods or services;
>
> (2) the cause of action arises from a statement or conduct by that person consisting of representations of fact [can be omission or half-truth] about that person's or a business competitor's business operations, goods, or services;
>
> (3) the statement or conduct was made either for the purpose of obtaining approval for, promoting, or securing sales or leases of, or commercial transactions in, the person's goods or services or in the course of delivering the person's goods or services; and
>
> (4) the intended audience for the statement or conduct meets the definition set forth in section 425.17(c)(2).

[5] 28 U.S.C. § 1334 provides in relevant part:

> (a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.
>
> . . .
>
> (e) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction - (1) of all of the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate; . . . .

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Weiland Sliding Doors & Windows, Inc. v. Panda Windows & Doors, LLC, 814 F. Supp. 2d 1033, 1037 (S.D. Cal. 2011) (citing *Simpson Strong-Tie Co. v. Gore*, 49 Cal. 4th 12, 30 (2010) (addressing elements related to commercial exemption from anti-SLAPP under section 425.17(c))); *see also JAMS, Inc. v. Superior Court*, 1 Cal. App. 5th 984, 995 (2016) ("Neither the *Kasky* decision nor the legislative history indicates the content of commercial speech must be an affirmative or positive representation, as opposed to an omission or half-truth.") (citing *Kasky v. Nike, Inc.*, 27 Cal. 4th 939 (2002)); *E.D.C. Techs., Inc. v. Seidel*, 225 F. Supp. 3d 1058, 1065 (N.D. Cal. 2016).

Each of the four commercial activity elements set forth in *Simpson Strong-Tie* and *Weiland* are satisfied here. ***First***, "goods" and "services" are defined broadly for purposes of the commercial exemption. *See JAMS, Inc.*, 1 Cal. App. 5th at 995 (applying commercial exemption to statements about mediation services); *Demetriades v. Yelp, Inc.*, 228 Cal. App. 4th 294, 307 (2014) (applying commercial exemption to statements about Yelp's review filter). Here, Defendants are primarily engaged in the business of providing health care services. *See* RJN, Ex. GG (Compl., ¶¶ 41, 67-68), *quoting* August 13, 2018 Offer Letter ("SGM and its associated and affiliated companies (collectively, the "SGM Companies") currently own, operate and/or manage several healthcare companies […] The SGM Companies also own and operate various ancillary providers."); RJN, Ex. GG (Compl. ¶ 68) (August 27, 2019 Transcript, at 13:1-16:3) ("SGM, our acquisition entity, will be a part of KPC […] KPC is an integrated healthcare system. We operate seven acute care hospitals […] In the ancillary side […] we also own and operate seven long-term acute care hospitals."); RJN, Ex. GG (Compl. ¶ 67) (August 26, 2019 Transcript, at 12:2-14:21) ("We come to the table with vast experience in operating safety net hospitals").

Second, *JAMS, Inc. v. Superior Court* is instructive as the causes of action against defendant JAMS arose from misleading or omitted statements regarding the qualifications of a JAMS neutral to act as a private judge for divorce proceedings. The *JAMS, Inc.* court expounded on the type of statements that are "representations of fact for purposes of analyzing the commercial nature of the speech." *JAMS, Inc.*, 1 Cal. App. 5th at 995. What matters for purposes of the commercial speech analysis is "whether the speech is intended to induce a commercial transaction, and whether the intended audience includes an actual or potential buyer for the goods or services." *Id.* at 995.

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Statements that are "certainly intended to be relied upon by its customers of its services" are representations of fact for the purpose of "analyzing the commercial nature of the speech." *Id.* at 995. The *JAMS, Inc.* court found that the representations made in the neutral's biography and general statements made by JAMS such as "'[e]verything we do and say will reflect the highest ethical and moral standards"' and that JAMS is "'dedicated to neutrality, integrity, honesty, accountability, and mutual respect in all our interactions,"' were commercial speech. The court concluded that "[t]hese representations published on a Web site to induce litigants to engage in ADR services offered by JAMS were commercial speech for purposes of section 425.17." *Id.*

To the extent the complaint is based on communications, they were either representations about Defendants' capabilities with respect to their own operations and services, or representations regarding the success or failure of the Debtors business operations. Specifically, Defendants represented that they would assume operations of the Verity Hospitals pursuant to the terms of the APA, and provide health care services to the communities they serve. *See* RJN, Ex. GG (Compl., ¶¶ 40, 44-46, 54). Defendants touted their special ability to assume responsibility for operating distressed hospitals. *Id.*, ¶¶ 41, 67-69. They further provided a letter regarding the asserted availability of certain liquidity needed to fund the APA sale transaction. *Id.*, ¶ 42.

Third, commercial speech arises where a "statement . . . was made either for the purpose of obtaining approval for, [or] promoting . . . commercial transactions in, the person's goods or services." Code Civ. Proc. § 425.17(c)(1). Defendants made the foregoing representations to persuade Plaintiffs to accept the SGM bid and ultimately to obtain approval for the transaction. *See Weiland Sliding Doors & Windows, Inc. v. Panda Windows & Doors*, LLC, 814 F. Supp. 2d 1033, 1037 (S.D. Cal. 2011) ("for the purpose of obtaining approval for […] the person's goods or services."); *JAMS, Inc.*, 1 Cal. App. 5th at 996 ("representations published […] to induce litigants to engage in […] services offered by JAMS were commercial speech for purposes of section 425.17.").

Fourth, the "intended audience" must be "an actual or potential buyer or customer, or a person likely to repeat the statement to, or otherwise influence, an actual or potential buyer or customer, or the statement or conduct arose out of or within the context of a regulatory approval

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process, proceeding, or investigation […]." Code Civ. Proc. § 425.17(c)(2).[6] Plaintiffs, as the Debtors, were the ones selecting which bid to accept and were likely to repeat Defendants' representations to patients and the communities served by the Hospitals as well as the Bankruptcy Court.

In sum, the commercial exemption under Section 425.17(c) is satisfied here. Accordingly, the anti-SLAPP statute does not apply, and any order to that effect is not subject to interlocutory review.

C. Defendants Have Not Met Their Burden Of Proving The Gravamen Of The Complaint Arises Out Of Protected Activity

Even if not commercial speech exempted from the anti-SLAPP statute, Defendants have not satisfied their burden of demonstrating the Complaint arises from "petitioning activity" protected by the anti-SLAPP statute. The statute defines "petitioning activity," or "an act in furtherance of [the] right of petition or free speech . . . in connection with a public issue," as:

> (1) any written or oral statement or writing made before a legislative, executive, or judicial proceeding, or any other official proceeding authorized by law;
>
> (2) any written or oral statement or writing made in connection with an issue under consideration or review by a legislative, executive, or judicial body, or any other official proceeding authorized by law;
>
> (3) any written or oral statement or writing made in a place open to the public or a public forum in connection with an issue of public interest;
>
> (4) or any other conduct in furtherance of the exercise of the constitutional right of petition or the constitutional right of free speech in connection with a public issue or an issue of public interest.

[6] Considering the enactment of section 425.17(c)(2), the California legislature presciently explained:

> SB 515 indeed borrows from the Kasky v. Nike formulation of commercial speech in the provision stating that a statement or conduct consisting of ***representations of fact about the person's business or its operations that arose out of or within the context of a regulatory approval process, proceeding or investigation, is deemed commercial speech*** and activity, and outside the protections of the anti-SLAPP law, even if that conduct or statement concerns an important public issue. (Kasky v. Nike, supra.)

Cal. Bill An., S.B. 515 Sen. (May 6, 2003) (emphasis added).

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Code Civ. Proc. § 425.16(e).

In determining whether a cause of action "arises from" a protected activity, a court looks to its "principal thrust or gravamen." *Ramona Unified School Dist. v. Tsiknas*, 135 Cal. App. 4th 510, 519-20 (2005); *see also Feldman v. 1100 Park Lane Associates*, 160 Cal. App. 4th 1467, 1478 (2008) ("The anti-SLAPP statute's definitional focus is not the form of the plaintiff's cause of action but, rather, the defendant's activity that gives rise to his or her asserted liability—and whether that activity constitutes protected speech or petitioning."). As the California Supreme Court explained in *Park v. Board of Trustees of California State University*, 2 Cal.5th 1057, 1060 (2017):

> [A] claim is not subject to a motion to strike simply because it contests an action or decision that was arrived at following speech or petitioning activity, or that was thereafter communicated by means of speech or petitioning activity. Rather, a claim may be struck only if the speech or petitioning activity itself is the wrong complained of, and not just evidence of liability or a step leading to some different act for which liability is asserted.

Id. at 1060.

This requires courts to "'distinguish between (1) speech or petitioning activity that is mere evidence related to liability and (2) liability that is based on speech or petitioning activity.'" *Id.* at 1065. Courts must "respect the distinction between activities that form the basis for a claim and those that merely lead to the liability-creating activity or provide evidentiary support for the claim." *Id.* at 1064. "'[T]he mere fact that an action was filed after protected activity took place" (*id.* at 1063), or the fact that a cause of action "may have been triggered by protected activity" (*See also City of Cotati v. Cashman*, 29 Cal. 4th 69, 78 (2002), or the "fact that protected activity may lurk in the background—and may explain why the rift between the parties arose in the first place" (*Episcopal Church Cases*, 45 Cal. 4th 467, 478 (2009)), does not mean a complaint *arises from protected activity*. Instead, courts consider "the principal thrust or gravamen of a plaintiff's cause of action" to determine whether the acts underlying that cause of action were acts in furtherance of the right of petition or free speech. *Ramona Unified School Dist. v. Tsiknas,* 135 Cal. App. 4th 510, 519-520 (2005); *see also Jordan-Benel v. Universal City Studios, Inc.,* 859 F. 3d 1184, 1191 (9th Cir.) ("for purposes of anti-SLAPP, the conduct from which a claim arises is the conduct that constitutes the specific act of wrongdoing challenged by the plaintiff").

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Here, the "principal thrust or gravamen" of the Complaint is Defendants' failure to perform their obligations in connection with a commercial sale transaction, and a course of conduct designed to trap Plaintiffs into that transaction and then coerce a re-trade. As a matter of law, this is not petitioning activity protected by the anti-SLAPP statute. Defendants utterly fail to articulate how the "principal thrust or gravamen" of Verity's Complaint "arises from" protected speech or petitioning activities. Relying on a case involving post-bankruptcy state court foreclosure litigation, *Crossroads Investors, L.P. v. Federal National Mortgage Assn*., 13 Cal. App. 5th 757, 781 (2017), Defendants contend the mere fact that that their wrongful and fraudulent conduct was directed to a debtor in bankruptcy necessarily means that it was protected petitioning activity. But, following Defendant's flawed logic, all putative purchasers in California bankruptcy sales proceedings would be insulated from wrongful and fraudulent conduct to the extent of any statements or representations made during the bidding and closing phases of the approval process.

As explained in *Valuerock TN Properties, LLC v. PKII Larwin Square, SC LP,* 36 Cal. App. 5th 1037 (2019), although a cause of action may have some factual relationship to litigation, it does not necessary follow that the claim "arises from" such protected activity. In *Valuerock,* a proposed assignor and assignee filed suit against a landlord over the landlord's failure to consent to the lease assignment request. During the litigation, the landlord rejected an amended lease assignment request, in response to which the plaintiffs filed an amended complaint based on such conduct. The Court of Appeal rejected the landlord anti-SLAPP motion, ruling that the "principal thrust or gravamen" of the amended complaint involved the landlord's failure to consent to the proposed assignment, not litigation conduct or communications. *Id*. at 1048. The court explained, "[t]o be sure, Defendants withheld consent to the amended assignment request during the litigation, which presumably prompted the filing of the second amended complaint. But that is not to say the second amended complaint was based on Defendants' litigation conduct." *Id.*; *see also USA Waste of Cal., Inc. v. City of Irwindale,* 184 Cal. App. 4th 53, 63 (2010) (gravamen of a cause of action seeking declaration of applicable governmental standards was not the fact that the City had issued of a Notice of Violation alleging violations of such standards, and the fact that the City's Notice was a factor for the filing of or incidental to the cause of action does not subject cause of action to anti-

SLAPP statute); *Navellier v. Sletten*, 29 Cal. 4th 82, 89 (2002) ("[T]hat a cause of action arguably may have been 'triggered' by protected activity does not [mean that] it is one arising from such."); *Graffiti Protective Coatings, Inc. v. City of Pico Rivera*, 181 Cal. App. 4th 1207, 1218 (2010) (complaint did not arise from protected activity, even though it involved statements that occurred in connection with official proceeding).

Here, as in *Valuerock,* the underlying events may have occurred contemporaneously with a legal proceeding (the bankruptcy), but they *do not arise* from petitioning activity in that proceeding, and the anti-SLAPP statute has no application.

1. The Gravamen Of The Contract Claim Is Not Petitioning Activity

The gravamen of Plaintiffs' first claim, for breach of contract, is that Defendants breached the APA by failing to close the transaction at the purchase price of $610 million and failing to have the financial wherewithal to do so, despite their contractual representation and warranty to the contrary in the APA. *See* RJN, Ex. GG (Compl., ¶¶ 42, 58, 82, 100, Ex. A, § 3.9). The APA also imposed obligations to cooperate in the transfer of operations, which defendants also violated through their conduct. *See* RJN, Ex. GG (Compl., ¶¶ 78-81, 100, Ex. A, §§ 4.2.1, 8.6, 12.17). Finally, the APA required Defendants to "cooperate in any efforts to render the Supplemental Sale Order a final, non-appealable order…," which Defendants breached by filing a notice of appeal of the Supplemental Sale Order and attempting to invoke a non-existent "Evaluation Period," ultimately leading to their failure to close the sale. *See* RJN, Ex. GG (Compl., ¶¶ 93, 100, Ex. A, § 8.6).

Hence, the "principle thrust or gravamen" of the contract claim is a course of conduct that resulted in a failure to close a hospital sale transaction, not petitioning activity. Any allegations about communications relating to the bankruptcy proceeding provide context for the actual controversy that is at the heart of this case: a commercial dispute.[7] As a matter of law, the failure

[7] If the Court concludes any of the allegations in the Complaint trigger the anti-SLAPP statute, Plaintiffs respectfully request leave to amend. *See Verizon Delaware, Inc. v. Covad Communications Co.,* 377 F.3d 1081, 1091 (9th Cir. 2004) ("granting a defendant's anti-SLAPP motion to strike a plaintiff's initial complaint without granting the plaintiff leave to amend would directly collide with Fed. R. Civ. P. 15(a)'s policy favoring liberal amendment."); *Brown v. Rawson-Neal Psychiatric Hosp.*, 840 F.3d 1146, 1152 (9th Cir. 2016) (quoting Fed. R. Civ. P. 8(d)(2) ("A party may set out 2 or more statements of a claim or defense

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to close a commercial transaction is not communicative conduct in furtherance of free speech. *See Jordan-Benel v. Universal City Studios, Inc.,* 859 F. 3d 1184, 1193 (9th Cir.) ("limiting the application of anti-SLAPP to claims that actually challenge free speech activity does not create an impermissible intent-to-chill requirement").

2. The Gravamen Of The Promissory Fraud Claim Is Not Petitioning Activity

The "principle thrust or gravamen" of the second claim, for promissory fraud, is that Defendants submitted a bid and then signed the APA on January 8, 2019, promising to pay $610 million for the Hospitals, while having had no intention of performing in accordance with the APA. *See* RJN, Ex. GG (Compl., ¶¶ 41, 44). Contrary to Defendants' assertions, these false promises were not made in the context of the bankruptcy proceeding: they were made outside the judicial process by a stranger to the proceeding.

Defendants fails to cite a single case applying the anti-SLAPP statute in such circumstances. Instead, they rely on cases challenging communications made by parties to litigation in pleadings, discovery responses, or in court. *See Suarez v. Trigg Labs,* 3 Cal. App. 5th 118, 125 (2016) (party to litigation failed to disclose fact to another party in litigation during settlement negotiations); *Nevallier v. Sletton,* 29 Cal. 4th 82, 89 (2002) (party to litigation made false statement to another party to litigation); *Fremont Reorganizing Corp. v. Faigin,* 198 Cal. App. 4th 1153, 1167 (2011) (statement made to Insurance Commissioner involved petitioning activity); *Graham-Sult v. Clainos,* 738 F.3d 1131, 1142-1143 (9th Cir. 2013) (statements made to probate court by attorney for executor of estate and trustees); *Crossroads Investors L.P. v. Federal National Mortgage Ass'n,* 13 Cal. App. 5th 757, 781 (2017) (statements made by creditor in discovery responses and settlement discussions in bankruptcy proceeding).

Here, Defendants' false promise was made outside the bankruptcy proceeding, in private commercial interactions with Plaintiffs. Defendants are not parties to the bankruptcy proceeding, and certainly were not "participants authorized by law" when the false promises were made. *See In re HST Gathering Co.,* 125 B.R. 466, 468 (W.D. Tex. 1991) (entity that desired to purchase

alternatively or hypothetically, either in a single count or defense or in separate ones. If a party makes alternative statements, the pleading is sufficient if any one of them is sufficient.").

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assets of the estate is not within the "zone of interests intended to be protected" under the bankruptcy statutes and regulations); *In re Nepsco, Inc.,* 36 B.R. 25 (Bankr.D.Me. 1983) (*accord*).

3. The Gravamen Of The Implied Contract/Implied Covenant Claim Is Not Petitioning Activity

The third claim for relief is based on the same conduct at issue in the breach of contract claim, but pled under an alternative legal theory. *See* RJN, Ex. GG (Compl., ¶¶ 100, 107). *Brown v. Rawson-Neal Psychiatric Hosp.,* 840 F.3d 1146, 1152 (9th Cir. 2016) ("A party may set out 2 or more statements of a claim or defense alternatively or hypothetically, either in a single count or defense or in separate ones. If a party makes alternative statements, the pleading is sufficient if any one of them is sufficient."). For the same reasons discussed above in connection with the contract claim, this claim does not fall within the anti-SLAPP purview.

D. Plaintiffs Are Likely to Prevail Under FRCP 12(b)(6)

As demonstrated in the prior section, Defendants' anti-SLAPP motion should be denied because they have failed to satisfy their burden of proving that the "gravamen" of this suit arises from protected activity. Even if Defendants had satisfied their burden of establishing that Plaintiffs' Complaint falls within the purview of the anti-SLAPP statute (which they have not), Plaintiffs can demonstrate the existence of well pled legal claims and thus a likelihood of success under the applicable Federal Rule of Civil Procedure 12(b)(6) standard. (Motion to Strike, p. 3, n. 2, *citing Planned Parenthood Fed's of Am. v. Center for Medical Progress,* 890 F. 3d 828, 834 (9th Cir.), *amended*, 897 F.3d 1224 (9th Cir. 2018), and *cert. denied sub nom. Ctr. For Med. Progress v. Planned Parenthood Fed'n of Am.,* 139 S. Ct. 1446, 203 L. Ed. 2d 681 (2019)).

1. Section 8.7 Of The APA Does Not Bar The Complaint

Defendants assert that Plaintiffs cannot recover on any claim for relief because Section 8.7 of the APA allegedly was not satisfied. Defendants are wrong, for many reasons.

Section 8.7 was plainly satisfied here. It provides as follows:

> 8.7 Medicare and Medi-Cal Provider Agreements. Sellers shall transfer their Medicare provider agreements pursuant to a settlement agreement with the Centers for Medicare and Medicaid Services ("CMS") and shall transfer their Medi-Cal provider agreements pursuant to a settlement agreement with the California Department of Health Care Services

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> ("DHCS"), which such settlement agreements shall result in: (i) resolution of all outstanding financial defaults under any of Sellers' Medicare and Medi-Cal provider agreements and (ii) full satisfaction, discharge, and release of any claims under the Medicare or Medi-Cal provider agreements, whether known or unknown, that CMS or DHCS, as applicable, has against the Seller or Purchaser for monetary liability arising under the Medicare or Medi-Cal provider agreements before the Effective Time; provided, however, that Purchaser acknowledges that it will succeed to the quality history associated with the relevant Medicare or Medi-Cal provider agreements assigned and shall be treated, for purposed of survey and certification issues as if it is the relevant Seller and no change of ownership occurred.

Further, Section 8.4 of the APA provides:

> 8.4 Performance of Covenants. Sellers shall have in all material respects performed or complied with each and all of the obligations, covenants, agreements and conditions required to be performed or complied with by Sellers on or prior to the Closing Date; provided, however, this condition will be deemed to be satisfied unless (a) Sellers were given written notice of such failure to perform or comply and did not or could not cure such failure to perform or comply within fifteen (15) business days after receipt of such notice and (b) the respects in which such obligations, covenants, agreements and conditions have not been performed have had or would have a Material Adverse Effect.
>
> [Emphasis added.]

Here, in accordance with Section 8.7, the Debtors obtained a settlement with the Centers for Medicare and Medicaid Services providing for the transfer of their Medicare Provider Agreements to SGM on November 19, 2019. *See* RJN, Ex. O, Docket No. 3680. With respect to the transfer of the Medi-Cal Provider Agreement between the Debtors and the California Department of Health Care Services ("DHCS") to SGM, the Debtors materially complied with their obligation to be in a position to transfer their Medi-Cal Provider Agreements to SGM with a "full satisfaction, discharge, and release of any claims under the … Medi-Cal provider agreements, whether known or unknown, that … DHCS … has against [SGM] for monetary liability arising under the … Medi-Cal provider agreements before the Effective Time," in other words, without successor liability.

First, on September 26, 2019, the Court entered its Memorandum Opinion [Docket No. 3146] (the "Memorandum Opinion"), which expressly held that the Medi-Cal "Provider Agreements may be sold free and clear of the liabilities which DHCS contends attach to the Provider Agreements. *See* RJN, Ex. LL. This includes the alleged liabilities for approximately $30

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million in unpaid HQA Fees and $25 million in Medi-Cal overpayments." Second, the Debtors secured an Order [Docket No. 3372] (the "Medi-Cal Provider Agreement Transfer Order") from the Bankruptcy Court authorizing the transfer of the Medi-Cal Provider Agreement free and clear of any interests asserted by DHCS. *See* RJN, Ex. Q. That order expressly provided:

> DHCS shall not adjust, offset or lien any payments owing to SGM and other SGM affiliates (collectively, "SGM Buyers") which are assigned any rights in connection with the transfer of the Medi-Cal Provider Agreements … and the SGM acquisition of the Hospitals and St. Vincent Dialysis Center (collectively, the "Assets") pursuant to the Sale Motion ("SGM Sale") after the transfer of the Assets (the "Transfer Effective Date"), or make any claims against any of the SGM Buyers or any of their assets, including, without limitation, any assets acquired by any of the SGM Buyers pursuant to the SGM Sale, for any obligations, liabilities, claims or other interests against the Debtors related to periods on or before the Transfer Effective Date ("Pre-Transfer Effective Date Liabilities") including without limitation for Pre-Transfer Effective Date Liabilities under or related to (a) the Medi-Cal Program, and (b) without prejudice to the rights of the Debtors or the SGM Buyers as provided for in the Asset Purchase Agreement [Docket No. 2305-1] by and among the Debtors and SGM, the Hospital Quality Assurance Fees Program, California Welfare & Institutions Code, § 14169.52(a) et. seq. or similar or successor statutes ("HQA Fee Program").

Further, although the Medi-Cal Provider Agreement Transfer Order did not address or resolve Medi-Cal's recoupment rights, if any, against SGM, that was unnecessary because those rights had previously been resolved in Sale Order. *See* RJN, Ex. E. In the Sale Order, which is long since final and was never appealed by DHCS, "recoupment" rights by all creditors, including DHCS, were expressly extinguished as to SGM.

Those Orders afforded equal or greater protection to SGM than any settlement could have, thereby satisfying Section 8.7. Contrary to Defendants' assertion, a settlement agreement was not the only means of satisfying Section 8.7. Rather, Section 8.4 of the APA provides:

> **8.4 Performance of Covenants.** Sellers shall have in all material respects performed or complied with each and all of the obligations, covenants, agreements and conditions required to be performed or complied with by Sellers on or prior to the Closing Date; provided, however, this condition will be deemed to be satisfied unless (a) Sellers were given written notice of such failure to perform or comply and did not or could not cure such failure to perform or comply within fifteen (15) business days after receipt of such notice and (b) the respects in which such obligations, covenants, agreements and conditions have not been performed have had or would have a

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Material Adverse Effect.

The Court has "exclusive jurisdiction to interpret, construe, and enforce the provisions of the APA and this Sale Order in all respects," and has determined that the Debtors' have satisfied Section 8.7. In its November 27, 2019 Order, the Court ruled that: "[t]he Debtors materially complied with Article 8.7 by obtaining an order authorizing the transfer of the Medi-Cal Provider Agreements free and clear of any interest asserted by the DHCS" and that "Debtors obtained a settlement with the Centers for Medicare and Medicaid Services providing for the transfer of their Medicare Provider Agreements to SGM, thereby satisfying their remaining obligations under Article 8.7 of the APA." RJN, Ex. AA. Defendants' assertions to the contrary are meritless.

In any event, given SGM's continued objection to the sufficiency of the Court's prior Orders, the Debtors reached a settlement agreement in principle with DHCS to the same effect on November 22, 2019. *See* RJN, Ex. Y, Nov. 26, 2019 Hr'g Tr. at 10:18-24. The APA did not require a written agreement or a Court approved agreement, so that an oral agreement as to terms expressly satisfied the terms and requirements of Section 8.7, even though they had been previously materially satisfied. Even if the Court's prior Orders regarding the Medi-Cal Provider Agreements were somehow insufficient to satisfy Section 8.7 (which Plaintiffs dispute), it would simply mean that the mandatory Closing Date for the transaction would have been a few days later, *i.e.,* ten days from the date a settlement was reached with DHCS. The DHCS settlement agreement was filed with the Court on December 9, 2019. Even assuming that agreement was a prerequisite to closing, the APA then required that the close occur "no later than 10 days" later, which would have been December 23, 2019. *See* RJN, Ex. GG (Compl., ¶ 46, Ex. A, § 1.3). Defendants, however, failed to close and the APA terminated four days later, on December 27, 2019.

Defendants appear to suggest that Plaintiffs had an obligation to issue a new "notice of closing" under the APA once the DHCS settlement agreement was filed on December 9, 2019. (Motion to Strike, pp. 16, 19.) The APA contains no such requirement. Instead, the APA states the "Closing Date" shall occur "no later than 10 days following the satisfaction or waiver of the closing conditions" to close, not 10 days following any notice. *See* RJN, Ex. GG (Compl., ¶ 46,

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Ex. A, § 1.3).[8] Further, the Defendants make no excuse for their failure to close 10 days after the settlement was filed publicly with the Court. Accordingly, there is no merit to whatsoever to Defendants' suggestion that Plaintiffs were obligated to issue closing notices under the APA.

Finally, in a footnote, Defendants suggest that the DHCS settlement was somehow deficient because it allegedly "did not release all known and unknown claims as required by Section 8.7." (Motion to Strike, p. 20, n. 4.) The assertion is simply false. Paragraph 2.8 of the settlement agreement provides for, among other things, the release "any and all claims . . . whether such claims are known or unknown." RJN, Ex. R (Docket No. 3786, p. 16) (emphasis added).

In sum, Plaintiffs claims do not fail as a matter of law under Section 8.7. Defendants flagrantly breached their obligation to close, and the Adversary Proceeding provides the forum for Plaintiffs to be compensated for the substantial losses they incurred as a result of Defendants' wrongful conduct.

2. The Litigation Privilege Does Not Shield Defendants From Liability For Breaching The APA

Defendants next assert that the litigation privilege under California Civil Code section 47(b) immunizes them from contract liability for any conduct they contend was not "clearly prohibit[ed]" by the APA. Not so.

Defendants fundamentally mischaracterize the test for application of the litigation privilege. As reflected in their own cited cases, the "purpose of the litigation privilege is to afford litigants and witnesses freedom of access to the courts [. . . and] to protect citizens from the threat of litigation for communications to government agencies whose function it is to investigate and remedy wrongdoing." *See McNair v. City & County of San Francisco,* 5 Cal. App. 5th 1154, 1162-11163 (2016) (quoting *People ex rel. Gallegos v. Pac. Lumber Co.*, 158 Cal. App. 4th 950, 958 (2008), as modified (Feb. 1, 2008) (internal quotations omitted). Not surprisingly, the privilege generally does *not* apply to contract claims. *See Vivian v. Labrucherie,* 214 Cal. App. 4th 267, 275-76 (2013). Rather, the starting point in the analysis is whether Defendants have been sued over a

[8] Plaintiffs' letter advising that the transaction should close by December 5, 2019 was not required by the APA.

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communication that was "(1) made in judicial or quasi-judicial proceedings; (2) by litigants or other participants authorized by law; (3) to achieve the objects of the litigation; and (4) that have some connection or logical relation to the action." *McNair,* 5 Cal. App. 5th at 1162 (*citing Silberg v. Anderson,* 50 Cal. 3d 205, 212 (1990)).

Here, Plaintiffs' breach of contract claim is not based solely on Defendants' communications directed to the Bankruptcy Court. Rather, they have been sued over a course of conduct designed to lock Plaintiffs into the APA with which Defendants had no intention of complying and did not comply. California law is settled that the litigation privilege does not bar liability for wrongful courses of conduct. *See Stacy & Witbeck, Inc. v. City and County of San Francisco,* 47 Cal. App. 4th 1, 8 (1996). In particular, "[t]he litigation privilege was never meant to spin out from judicial action a party's performance and course of conduct under a contract." *Id.* Hence, the possibility that some of the conduct constituting a breach of contract may have been communicative is irrelevant because it was part of any overarching scheme and course of conduct designed to breach the APA." *See also Wentland v. Wass,* 126 Cal. App. 4th 1484, 1494 (2005) (litigation privilege did not protect statements made in the course of litigation that breached a confidentiality agreement). This includes Plaintiffs' allegation that Defendants breached the APA by improperly filing an appeal from the Court's AG Conditions Order, in violation § 8.6 of the APA. Where a contract prohibits certain litigation conduct, breach of such a contract is not privileged. *See Nevallier v. Sletton,* 29 Cal. 4th 82, 97-98 (2002) (litigation privilege did not apply to act of filing lawsuit in breach of agreement); *see also Wentland*, 126 Cal. App. 4th at 1494.

Moreover, no case law supports Defendants' sweeping proposition that all interactions with parties to a bankruptcy proceeding are cloaked in the litigation privilege. Indeed, the court in *In re Morpheus Lights, Inc.,* 228 B.R. 449, 455–56 (Bankr. N.D. Cal. 1998), rejected precisely such a proposition. The debtor sued its lender and the lender's president for breach of fiduciary duty and unfair competition based on allegations that they " engaged in a pattern of improper post-petition conduct [. . . and] have taken control of the debtor and the bankruptcy case for their own benefit. *Id.* at 452. In declining to apply the litigation privilege, the court held "the crux of the allegations against [defendant] is that it has exceeded its role as a mere lender to the debtor and has exercised

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control through a pattern of wrongful acts and unfair practices which has injured the debtor, creditors and estate. This type of conduct is separate and distinct from conduct typically found within even the most litigious court proceedings. The litigation privilege does not bar suits addressing such injurious conduct." *Id.* at 455–56.

Finally, Plaintiffs' cited cases are distinguishable because they involved claims premised on communications made by the defendant to a court or regulatory agency. *See McNair*, 5 Cal. App. 5th 1154 (defendant sued for sending letter to Department of Motor Vehicles); *Vivian,* 214 Cal. App. 4th 267 (defendant sued over statements made to internal affairs investigator and to family court); *Feldman v. 1100 Park Lane Assocs.,* 160 Cal. App. 4th 1467, 1497-98 (2008) (defendant sued over filing of unlawful detainer action). In contrast, the Complaint here is not.

3. Verity Has A Likelihood Of Success On Its Claim For Promissory Fraud

a. The Litigation Privilege Is Inapplicable

Plaintiffs' second claim alleges that Defendants committed promissory fraud when Dr. Chaudhuri submitted a bid and then signed the APA on January 8, 2019, while Defendants had no intention of performing in accordance with the APA. After locking Plaintiffs into an APA that Defendants had no intention of performing, Defendants then dragged Plaintiffs through months of diminishing cash reserves without disclosing that they had no intention of ever closing the transaction for the price dictated by the APA. Defendants contend the litigation privilege protects them from liability for any false promise that was made in the context of a potential bankruptcy sale. Reduced to its essence, Defendants contend there can be no liability for defrauding debtors involved in a bankruptcy proceeding. No legal authority supports their bizarre and extreme position. Indeed, Defendants fail to cite a single case applying the litigation privilege to a claim of promissory fraud in any context.

As noted above, the litigation privilege only applies to statements "made in judicial or quasi-judicial proceeding" made "by litigants or other participants authorized by law." *Silberg,* 50 Cal. 3d at 212. Here, Defendants' false promises supporting the promissory fraud claim in private commercial interactions with Plaintiffs. Defendants are not parties in interest to the bankruptcy proceeding, and certainly were not "participants authorized by law" when the false

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promises were made. Indeed, when Defendants submitted their bid and signed the APA, they had never appeared in the bankruptcy court and were strangers to the proceedings. *See LiMandri v. Judkins,* 52 Cal. App. 4th 326, 345 (1997) (litigation privilege did not extend to defendants who filed a notice of lien in a lawsuit to which they were not parties); *Wise v. Thrifty Payless, Inc.,* 83 Cal. App. 4th 1296, 1306-1307 (2000) (litigation privilege did not extend to nonparty who communicate with party about issues related to litigation); *Gonzalez v. Compass Vision, Inc.*, 2010 WL 3783164, *5 (S.D. Cal. 2010) ("The [litigation] privilege does not extend infinitely back in time to protect every tortious act that might someday result in a communication in an official proceeding"); *see also In re HST Gathering Co.,* 125 B.R. 466, 468 (W.D. Tex. 1991) (entity that desired to purchase assets of the estate is not within the "zone of interests intended to be protected" under the bankruptcy statutes and regulations); *In re Nepsco, Inc.,* 36 B.R. 25 (Bankr.D.Me. 1983) (*accord*).

In addition, the litigation privilege only applies to communications that are made "to achieve the objects of the litigation." *See Silberg*, 50 Cal. 3d at 212. "That is to say, the communicative act—be it a document filed with the court, a letter between counsel or an oral statement—must function as a necessary or useful step in the litigation process and must serve its purposes." *Rothman v. Jackson,* 49 Cal. App. 4th 1134, 1146 (1996). Here, Defendants' fraudulent course of conduct designed to entrap Plaintiffs into an APA that Defendants had no intention of performing certainly did not "achieve the objects of the litigation."[9] It did just the opposite.

Finally, the litigation privilege does not apply to a "tortious course of conduct," which is precisely what is alleged in the Complaint in this case. *See LiMandri v. Judkins,* 52 Cal. App. 4th 326, 345 (1997) (litigation privilege did not bar claim for tortious interference with contract based on tortious course of conduct that included filing a lien in litigation); *Mancini & Assoc. v. Schwetz,* 39 Cal. App. 5th, 656, 661 (Ct. App. 2019), *as modified on denial of reh'g* (Sept. 30, 2019)

[9] Again, Defendants' cited cases are distinguishable. *Sacramento Brewing Co. v. Desmond, Miller & Desmond*, 75 Cal. App. 4th 1082, 1086 (1999), and *Shoemaker v. Siegel,* 2017 WL 3671154 (C.D. Cal. Aug. 25, 2017), involved claims based on statements contained made directly to the bankruptcy court. *Navarro v. IHOP Properties, Inc.*, 134 Cal. App. 4th 834 (2005), involved statements made to settle a lawsuit, not as part of a commercial transaction.

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("although Schwetz's act of executing the Memorandum was communicative, it was but one act in a course of tortious conduct to deprive Mancini of its attorney fees"); *Olszewski v. Scripps Health*, 30 Cal. 4th 798, 830 (2003) (privilege does not apply to tortious courses of conduct).

b. Plaintiffs Have Adequately Alleged Promissory Fraud

Defendants assert that Plaintiffs cannot establish the elements of promissory fraud because they have alleged that Defendants "never anticipated that Plaintiffs would obtain an agreement from the Attorney General" and "believed they would never be obligated to pay the full purchase price." (Mot., p. 22.) Defendants' position is a semantic ploy.

The Complaint contains detailed allegations about the parties' negotiations, Defendants' misrepresentations and omissions, and Defendants' fraudulent intent to cause Plaintiffs' to reasonably but detrimentally rely on Defendants' misrepresentations. The Complaint repeatedly alleges that Defendants had no intention of performing their obligation under the APA to pay the $610 million purchase. *See* RJN, Ex. GG (Compl. Preliminary Statement, ¶¶ 102, 107, 110). The *particular reason* Defendants had no such intention is not relevant. The bottom line is that they induced Plaintiffs to enter the agreement through the false promise that they Defendants would pay $610 million if and when the conditions were satisfied. The Court should reject Defendants' "attempt to override the clear statement[s] in Plaintiffs' complaint" because "Plaintiffs are 'master[s] of the complaint,'" not Defendants. *Santino v. Apple Inc.*, 2018 WL 2091491, at *2 (N.D. Cal. May 7, 2018) (quoting *Caterpillar Inc. v. Williams*, 482 U.S. 386, 398–99 (1987)); *see also Cruz v. Freedom Mortg. Corp.*, 2018 WL 6118532, at *4 (C.D. Cal. May 3, 2018), *reconsideration denied*, 2018 WL 5905389 (C.D. Cal. July 6, 2018) (rejecting argument that certain allegations "concede" that defendant's misrepresentations were not fraudulent, and finding "this mischaracterizes Plaintiff's allegations").

At the pleadings stage, the Court must accept as true Plaintiffs' factual allegations and all inferences to be derived from those allegations. Defendants' alleged belief that the fraud claim is "nonsensical" is irrelevant, and merely confirms the claim involves disputed factual issues. *See Polderman v. Gannett Co., Inc.*, 2009 WL 10673007, at *4 (S.D. Cal. Nov. 3, 2009) ("Because the Court must accept all well-pleaded factual allegations in the Complaint as true and Defendants'

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argument rests on disputed questions of fact, the Court finds that dismissal of this claim under Rule 12(b)(6) is not appropriate."); *Shropshire v. Fred Rappoport Co.*, 294 F. Supp. 2d 1085, 1099 (N.D. Cal. 2003) ("The Court is unable to resolve this issue at this stage of the proceeding, when no discovery has been permitted, because the applicability of the anti-SLAPP statute turns on disputed questions of fact.").

For the foregoing reasons, Plaintiffs have demonstrated a well pled fraud claim under the applicable Rule 12(b)(6) standard.

4. Verity Has A Likelihood Of Success On Claim For Tortious Breach of Contract (Breach of the Implied Covenant of Good Faith and Fair Dealing)

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. *See* RJN, Ex. GG (Compl., ¶¶ 100, 107). For the reasons discussed above, the litigation privilege does not apply to the course of conduct at issue in the third claim for relief. *See supra,* pp. 12-24.

Defendants also assert the third claim for relief is not cognizable under California law. Not so.[10] California "has a legitimate and compelling interest in preserving a business climate free of fraud and deceptive practices" and "a plaintiff advances the public interest in punishing intentional misrepresentations and in deterring such misrepresentations in the future." *Robinson Helicopter Co. v. Dana Corp.*, 34 Cal. 4th 979, 990-93 (2004) (internal quotations and alterations omitted). "Simply put, a contract is not a license allowing one party to cheat or defraud the other." *Id.* (quotations omitted). Accordingly, while "[a] breach of contract remedy assumes that the parties to a contract can negotiate the risk of loss occasioned by a breach," a "party to a contract cannot rationally calculate the possibility that the other party will deliberately misrepresent terms critical to that contract" and "[n]o rational party would enter into a contract anticipating that they are or

[10] The federal courts in this state recognize the existence of such a claim outside the insurance context. *See, e.g.*, *Vestis, LLC v. Caramel Sales, Ltd.*, 2019 WL 3312212, at *9 (C.D. Cal. Apr. 30, 2019); *Najor v. Wells Fargo Bank, N.A.*, 2019 WL 1858502, at *4 (S.D. Cal. Apr. 25, 2019); *Dairy v. Harry Shelton Livestock, LLC*, 2019 WL 631493, at *10 (N.D. Cal. Feb. 14, 2019); *Century of Progress Prods. v. Vivendi S.A.*, 2018 WL 4191340, at *9 (C.D. Cal. Aug. 28, 2018); *Kanter v. Playbill, Inc.*, 2017 WL 10591601, at *7 (C.D. Cal. Aug. 31, 2017); *Expedited Packages, LLC v. Beavex Inc.*, 2015 WL 13357436, at *3 (C.D. Cal. Sept. 10, 2015).

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will be lied to." *Id.* at 990–93 (quotations omitted). A tortious breach of contract "may be found when (1) the breach is accompanied by a traditional common law tort, such as fraud or conversion; (2) the means used to breach the contract are tortious, involving deceit or undue coercion; or (3) one party intentionally breaches the contract intending or knowing that such a breach will cause [. . .] substantial consequential damages." *Id.* (quotation omitted). Here, the Complaint alleges all three circumstances, which is more than sufficient to state a claim for relief under the applicable Rule 12(b)(6) standard.

As this Court previously observed, "[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and in its enforcement." *Las Vegas Land & Dev. Co., Inc. v. Bank of Am., N.A.*, 2018 WL 6991161, at *6 (C.D. Cal. Oct. 15, 2018) (quoting *Carma Developers, Inc. v. Marathon Development California, Inc.*, 2 Cal. 4th 342, 371 (1992)); *see* RJN, Ex. Y, Nov. 26, 2019 Hr'g Tr. at 14:17-20. "This duty, or covenant, finds particular application in situations where one party is invested with a discretionary power affecting the rights of another" and exists "to prevent one contracting party from unfairly frustrating the other party's right to receive the benefits of the agreement actually made," even if no express breach is ultimately established. *Las Vegas Land,* at *6 (quoting California cases). Defendants' fraudulent scheme to take advantage of community hospitals in dire financial distress is quintessential bad faith. *See id.*; *see also Sunfarms, LLC v. Eurus Energy Am. Inc.*, 2019 WL 4736223, at *6 (S.D. Cal. Sept. 27, 2019) (denying dismissal of implied covenant claim where defendants frustrated plaintiff's expectations of benefit by causing unreasonable delay, asserting unreasonable terms, and failing to respond to plaintiff); *Century of Progress Prods. v. Vivendi S.A.*, 2018 WL 4191340, at *10–13 (C.D. Cal. Aug. 28, 2018) (denying dismissal of tortious breach claim where defendants "allegedly engaged in separate nefarious accounting practices to conceal and underreport," which "imposed additional costs on Plaintiffs not reasonably within the parties' contemplation during contract formation[.]").

None of Defendants' cited cases address the rule set forth in *Robinson Helicopter*. Rather, Defendants' cited cases are either out of date, inapposite, or actually establish the viability of Plaintiffs' claim. For instance, in *Pension Tr. Fund for Operating Engineers v. Fed. Ins. Co.*, 307

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F.3d 944, 954–55 (9th Cir. 2002), the Ninth Circuit held that a party had adequately alleged facts supporting a cause of action for the tortious breach of the implied covenant of good faith and fair dealing where the opposing party owed a fiduciary duty by controlling the financially-dependent party in a manner that made the opposing party potentially liable. Similarly, the court in *Stop Loss Ins. Brokers, Inc. v. Brown & Toland Med. Grp.*, 143 Cal. App. 4th 1036, 1041 (2006), noted that "when the actions that constitute the breach violate a social policy that merits the imposition of tort remedies[,]" the cause of action exists. *Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 7 Cal. 4th 503, 514 (1994), is inapposite because it addressed a claim of tortious interference with contract brought against a party to the contract and a conspiracy to breach claim, neither of which is at issue here. Further, *Aas v. Superior Court*, 24 Cal. 4th 627(2000), has been superseded by statute. *See S. California Gas Leak Cases*, 7 Cal. 5th 391, 402 (2019). Defendants' remaining cases merely allowed tort recovery for a breach of the covenant of good faith and fair dealing is permitted where there is a special relationship between the parties. *See Denholm v. Houghton Mifflin Co.*, 912 F.2d 357, 361 (9th Cir. 1990); *Velazquez v. GMAC Mortg. Corp.*, 605 F. Supp. 2d 1049, 1072 (C.D. Cal. 2008); *California Joint Powers Ins. Auth. v. Munich Reinsurance Am., Inc.*, 2008 WL 1885754, at *2 (C.D. Cal. Apr. 21, 2008). None of these cases stands for the proposition that Defendants cannot face liability on the third claim for relief.

Plaintiffs' claim for tortious breach of the APA and its implied covenant of good faith and fair dealing, set forth in its third cause of action, is viable and properly pleaded.[11]

E. Plaintiffs' Alter Ego And Agency Allegations Are More Than Sufficient to Satisfy the Pleading Standard

Finally, Defendants make a handful of assertions challenging Plaintiffs' claims directed at the non-SGM Defendants. None has merit.

[11] Defendants assert in a footnote that Plaintiffs' third claim for relief is somehow duplicative of its breach of contract and fraud claims. As discussed above, such assertion is demonstrably incorrect. As with Defendants' other cases it relied on in purported support of its contentions, *Careau & Co. v. Sec. Pac. Bus. Credit, Inc.,* 222 Cal. App. 3d 1371, 1395 (1990), again demonstrates the existence of Plaintiffs' tortious breach claim under California law. In *Wilson v. Gateway, Inc.,* 2010 WL 11520532, at *3 (C.D. Cal. Jan. 25, 2010), the plaintiff did not even allege a tortious breach of contract claim, so Defendants' reliance thereon is misplaced.

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1. Defendants' "Known Related Entities" Case Law Is Inapposite

First, Defendants suggest there can be no alter ego liability on a contract claim. On the contrary, California courts have imposed such liability for years. *See, e.g.*, *Automotriz etc. De California v. Resnick,* 47 Cal. 2d 792 (1957). This is true even where the plaintiff knew of the alleged alter ego's existence at the time of contracting. *See G. E. J. Corp. v. Uranium Aire, Inc.*, 311 F.2d 749, 757 (9th Cir. 1962); *Hiehle v. Torrance Millworks, Inc.*, 126 Cal. App. 2d 624, 630 (1954).

G.E.J. Corp. v. Uranium Aire, Inc., 311 F.2d 749, 757 (9th Cir. 1962), is instructive. G.E.J. was a corporation organized by another corporation, M.F. Corporation, for the purpose of entering an option agreement for mining claims. Although G.E.J. was the signatory on the agreement, M.F. Corporation had given assurances that it would stand behind G.E.J. in the performance of the option agreement. *Id.* at 757. When G.E.J. breached the agreement, plaintiffs filed suit against both companies. The court found that M.F. Corporation was estopped to deny its liability on the contract. Where there misrepresentations induced a party to enter a transaction, considerations of "equity and fair dealing require the application of the alter-ego doctrine on [that party's] behalf" and "it would be unjust to allow MF to escape liability by operating through a puppet corporation organized with insufficient capital to meet its prospective liabilities." *Id.*

In *Hiehle v. Torrance Millworks, Inc.*, 126 Cal. App. 2d 624 (1954), a corporation borrowed money from the plaintiff, its bookkeeper. The amounts were not paid when due, and the plaintiff brought suit against both the corporation and its two stockholders. The court found the stockholders liable because "[i]t would be unjust to permit defendants to make use of [the corporate structure] to escape from their personal liability for its debts." *Id.* at 629. Although the plaintiff knew that he was contracting with the corporation rather than its stockholders, the latter fraudulently induced him to make the loans. *Id.* at 630. The *Heihle* court distinguished Defendants' cited case, *Lynch v. McDonald*, 155 Cal. 704 (1909), [12] because it "merely [held] that

[12] The facts in *Lynch* bear no resemblance to this case. The court declined to allow an attorney to pierce his client's corporate veil and hold its president and dominant shareholder, whom the attorney also represented, liable under his retention agreement. *Id.* at 705–706. However, the attorney not only knew of the alleged alter ego's existence—the attorney had advised him "in all business affairs" as corporate president and who "by years of association with [the president and dominant shareholder] and service for him and the company

the court may properly refuse to look beyond the corporation to the individuals who compose and control it where the plaintiff dealt with the corporation with full knowledge of the facts and where considerations of equity and fair dealing do not require application of the doctrine in his behalf."[13]

Here, Defendants 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. *See* RJN, Ex. GG (Compl. ¶¶ 67-69, August 26, 2019 Transcript, at 12:2-14:21; August 27, 2019 Transcript, at 13:1 -16:3, August 29, 2019 Transcript, at 12:9-16:3). Plaintiffs were induced to enter the transaction in part based on statements about KPC's experience in operating hospitals and their ability to secure financing. Because such misrepresentations were used to induce Plaintiffs to enter the transaction, considerations of "equity and fair dealing require the application of the alter-ego doctrine" as it would be it would be unjust to allow Defendants to escape liability by operating through a corporation organized with insufficient capital to meet its prospective liabilities.

2. Plaintiffs Have Alleged Sufficient Facts To Support Alter Ego Liability

Defendants next assert that Plaintiffs have failed to allege any factual basis for alter ego liability. Again, they are incorrect.

With respect to piercing the corporate veil to reach an individual, "California alter ego law requires proving two elements: 1) a unity of interest and ownership between the corporation and the individual; and 2) if acts by the corporation are treated as acts of the corporation alone, an inequitable result will follow." *Prompt Staffing, Inc. v. United States*, 321 F. Supp. 3d 1157, 1175–76 (C.D. Cal. 2018) (citing *Mesler v. Bragg Mgmt. Co.*, 39 Cal.3d 290 (1985)). With respect to piercing the corporate veil to reach related entities, "[a] court may also disregard the corporate form in order to hold one corporation liable for the debts of another affiliated corporation when the latter is so organized and controlled, and its affairs are so conducted, as to make it merely an

was thoroughly familiar with all the facts concerning the president's relation to the corporation." *Id* at 706. Here, Plaintiffs did not have any such intimate knowledge about Defendants' inner-workings.

[13] *Brunswick Corp. v. Waxman,*459 F. Supp. 1222 (E.D.N.Y. 1978), *aff'd* 599 F.2d 34 (2d Cir. 1979), is not binding authority and is distinguishable because New York follows the "instrumentality" rule to determine alter ego status. *See Lowendahl v. Baltimore & O.R. Co.,* 247 A.D. 144, 287 N.Y.S. 62, 76 (App. Div.), *aff'd*, 272 N.Y. 360, 6 N.E.2d 56 (1936). California does not.

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instrumentality, agency, conduit, or adjunct of another corporation." *Toho-Towa Co. v. Morgan Creek Prods., Inc.*, 217 Cal. App. 4th 1096, 1107–08, (2013) (quotations omitted). To determine a unity of interest between a corporation and an individual, California courts consider the following list of non-exhaustive, interrelated factors:

> [T]he commingling of funds and other assets; the failure to segregate funds of the individual and the corporation; the unauthorized diversion of corporate fluids to other than corporate purposes; the treatment by an individual of corporate assets as his own; the failure to seek authority to issue stock or issue stock under existing authorization; the representation by an individual that he is personally liable for corporate debts; the failure to maintain adequate corporate minutes or records; the intermingling of the individual and corporate records; the ownership of all the stock by a single individual or family; the domination or control of the corporation by the stockholders; the use of a single address for the individual and the corporation; the inadequacy of the corporation's capitalization; the use of the corporation as a mere conduit for an individual's business; the concealment of the ownership of the corporation; the disregard of formalities and the failure to maintain arm's-length transactions with the corporation; and the attempts to segregate liabilities to the corporation.

Prompt Staffing, Inc., 321 F. Supp. 3d at 1175–76 (quotation omitted). "No single factor is determinative," and courts must consider all the circumstances in deciding whether there is a unity of interest. *Id.* (quotation omitted). Relatedly, courts consider nearly identical factors in considering a "single business enterprise." *Toho-Towa Co.*, 217 Cal. App. 4th 1096, 1108–09 (2013) ("Factors for the trial court to consider include the commingling of funds and assets of the two entities, identical equitable ownership in the two entities, use of the same offices and employees, disregard of corporate formalities, identical directors and officers, and use of one as a mere shell or conduit for the affairs of the other.").

Here, while discovery in the Adversary Proceeding will reveal the full extent of Defendants' alter ego status, the allegations asserted in the Complaint establish the unity of interest among the Co-Defendants and SGM, as well as the single business enterprise in which the affiliated companies operated, and that they all participated in the Sale process as follows:

- Defendants shared corporate headquarters and/or common officers and directors, *see, e.g.*, RJN, Ex. GG, Compl. ¶¶ 12-17;
- The SGM offer was issued on letterhead that included the KPC logo and described the Defendants as a set of "affiliate companies," *see id.* at ¶ 41;

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- One of the Co-Defendants provided a proof of funds in support of the SGM bid, which was a material inducement to the Debtors' ultimate decision to request that the Court approve SGM as the successful bidder, *see id.* at ¶ 42;
- On December 14, 2018, a meeting was held between numerous representatives of the Defendants and the Debtors to discuss the Hospitals and Defendants' proposal to acquire them, *see id.* at ¶ 43;
- On February 6, 2019, the Bankruptcy Court held a hearing on the approval of the APA, during which counsel for SGM described SGM's affiliate relationship with "a larger organization called The KPC Group," *see* RJN, Ex. GG, Compl. ¶ 48;
- On March 11, 2019, SGM's General Counsel emailed the Debtors' investment banker requesting permission to populate "KPC's dataroom with Verity's confidential information" in order to provide access to "KPC's potential financing partners" *see id.* at ¶ 51;
- On May 17, 2019, Dr. Chaudhuri filed an Early Termination Notice with the Federal Trade Commission regarding the Sale, which lists the "Acquiring Party" as "Kali P. Chaudhuri, trustee" and the "Acquired Party" as "Verity Health System of California, Inc.", *see id.* at ¶ 55. The Defendants thereafter described the Sale on their websites as an acquisition by KPC and Chaudhuri, *see id.* at ¶¶ 56-57;
- Employees of KPC oversaw approximately 20 different workstreams to effectuate the Sale and met weekly with the Debtors to ensure a smooth transition of operations, *see id.* at ¶ 60;
- In August 2019, the Attorney General held public hearings at each Hospital to solicit comments regarding the Sale. A representative of the Defendants repeatedly made public statements that, while SGM is the acquisition arm of KPC, KPC and SGM are one and the same business entity led by Dr. Chaudhuri, *see id.* at ¶¶ 66-69; and
- Defendants secured a proposed term sheet stating, in part, that Co-Defendants would guarantee some or all of SGM's purchase of the Hospitals, *see id.* at ¶ 82.

The Co-Defendants were instrumentalities of SGM's wrongful conduct, both pre- and post-approval of the SGM Sale. The Co-Defendants were used in bad faith to evade Plaintiffs and SGM's financial obligations to Plaintiffs under the APA, indisputably creating an inequitable result. *See Prompt Staffing, Inc.*, 321 F. Supp. 3d at 1177–78. As such, an appropriate remedy for such wrongful conduct is a determination that SGM's contractual consent and misconduct are attributable to the Co-Defendants as its instrumentalities and with shared responsibility. *See, e.g.*, *Prompt Staffing, Inc.*, 321 F. Supp. 3d at 1178 (alter ego liability existed where individual owner asserted control over corporations, commingled funds and assets, treated corporate assets as his

own, and concealed ownership to evade creditors); *Toho-Towa Co.*, 217 Cal. App. 4th 1096, 1109 (2013) (business entities constituted a "single business enterprise" for purposes of alter ego liability where they had common ownership, exploited the same assets, had the same employees, and an affiliate entity would not have sufficient funds to pay its debts).

Ignoring the numerous allegations in the Complaint setting forth detailed facts about the alter ego status of defendants, Defendants also assert that Plaintiffs are not entitled to make certain allegations based on "on information and belief" and some "group" the misconduct of the Defendants. (Motion to Strike, pp. 31-32.) Contrary to Defendants' assertions, such allegations are entirely appropriate. *E.g.*, *Stewart v. Screen Gems-EMI Music, Inc.*, 81 F. Supp. 3d 938, 962–63 (N.D. Cal. 2015) (rejecting argument that "information and belief" allegations failed to plead alter ego, as the pleading "alleges specific facts regarding the nature of the relationship among Defendants and their foreign affiliates that are pertinent to assessing alter ego" and "Courts have found a unity of interest premised on even less."); *Vasic v. PatentHEALTH, L.L.C.*, 2014 WL 2159268, at *5 (S.D. Cal. May 22, 2014) (same); *see also In re Chrysler-Dodge-Jeep Ecodiesel Mktg., Sales Practices, & Prod. Liab. Litig.*, 295 F. Supp. 3d 927, 990 (N.D. Cal. 2018) (rejecting "lumping" dismissal argument of alter ego theory because "at this early stage in the proceedings, Plaintiffs have essentially been forced to lump the Bosch companies because the Bosch Defendants have chosen to operate a specific way[.]").

Defendants also make the bizarre assertion that Plaintiffs somehow "concede" that KPC Healthcare is not an alter ego for any of the other Co-Defendants in Paragraph 41 of the Complaint. (Motion to Strike, p. 32.) Paragraph 41 merely quotes the August 13, 2018 SGM offer. *See* RJN, Ex. GG (Compl. ¶ 41). It does not constitute any "concession" by Plaintiffs.

3. Plaintiffs' Agency And Conspiracy Claims Are Sufficient

Finally, Plaintiffs' conspiracy allegations should stand. As explained above, the Complaint more than adequately ties the Defendants to the underlying tortious and fraudulent conduct. *See, e.g.*, *Planned Parenthood Fed'n of Am., Inc. v. Ctr. for Med. Progress*, 214 F. Supp. 3d 808, 828–29 (N.D. Cal. 2016), *aff'd*, 890 F.3d 828 (9th Cir. 2018), amended, 897 F.3d 1224 (9th Cir. 2018), and *aff'd*, 735 F. App'x 241 (9th Cir. 2018) (rejecting argument that corporate entities, agents, and

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employees cannot conspire with themselves, finding "the allegations adequately identify and link each defendant, including Merritt, to the underlying tort they are alleged to either have committed directly or conspired to commit" and that the alter ego allegations do "not preclude the assertion of a conspiracy claim" at the pleadings stage and prior to discovery).[14] At the pleading stage, there is no basis to strike such claims for relief.

IV. RESERVATION OF RIGHTS

This Opposition relates solely to the Defendants' request to strike the Complaint as set forth in the Motion. As to the Defendants' alternative request for dismissal of the Complaint, the Defendants have not demonstrated an adequate basis to dismiss the Complaint, and the Debtors reserve all rights with respect to such arguments, which will be made in a separate opposition. Accordingly, nothing contained herein is intended or shall be construed as: (i) a waiver of the Debtors' or any appropriate party in interest's rights to dispute, object to, or otherwise challenge the substantive relief sought by the Defendants not otherwise set forth in the Motion; or (ii) a waiver of any claims, causes of action, defenses, objections, or other rights to respond which may exist against the Defendants.

V. CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that the Court deny Defendants' anti-SLAPP motion. In the event the Court is inclined to grant any portion of the motion, Plaintiffs respectfully request leave to amend.

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[14] Plaintiffs have properly pleaded that Defendants engaged in a civil conspiracy to induce breach of the APA, to tortiously breach the APA, and to breach the APA's implied covenant of good faith and fair dealing. "The elements of a civil conspiracy are '(1) the formation and operation of the conspiracy; (2) the wrongful act or acts done pursuant thereto; and (3) the damage resulting.'" *Sprint Nextel Corp. v. Thuc Ngo*, No. C-12-02764 CW EDL, 2012 WL 4127296, at *6 (N.D. Cal. Sept. 18, 2012), *report and recommendation adopted*, No. C 12-2764 CW, 2012 WL 4801629 (N.D. Cal. Oct. 9, 2012) (quoting *Mosier v. S. Cal. Physicians Ins. Exch.*, 63 Cal.App.4th 1022, 1028 (1998)). "[T]o properly allege a claim for conspiracy to induce breach of contract, Plaintiff must also allege that: (1) Plaintiff had a valid and existing contract; (2) Defendant had knowledge of the contract and intended to induce its breach; (3) the contract was in fact breached by the contracting party; (4) the breach was caused by Defendant's unjustified or wrongful conduct; and (5) Plaintiff has suffered damage." *Id.* (quoting *Dryden v. Tri–Valley Drowers*, 65 Cal.App.3d 990, 995 (1977)).

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