Docket #0056 Date Filed: 3/4/2020

SAMUEL R. MAIZEL (Bar No. 189301)
samuel.maizel@dentons.com
SONIA R. MARTIN (Bar No. 191148)
sonia.martin@dentons.com
TANIA M. MOYRON (Bar No. 235736)
tania.moyron@dentons.com
NICHOLAS A. KOFFROTH (Bar. No. 287854)
nicholas.koffroth@dentons.com
DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
Tel: (213) 623-9300 / Fax: (213) 623-9924

Attorneys for the Chapter 11 Debtors and Debtors In Possession

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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' MOTION TO DISMISS PLAINTIFF'S COMPLAINT

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

1820151200305000000000004

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.

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

TABLE OF CONTENTS

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

TABLE OF AUTHORITIES

Page(s)

Cases

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Statutes

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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 (collectively, the "Debtors" or "Plaintiffs"), submit this opposition (the "Opposition") to the *Motion to Dismiss Plaintiffs' Complaint* (the "Motion") [Docket No. 40] filed by Defendants Kali P. Chaudhuri, M.D. ("Chaudhuri"), Strategic Global Management, Inc. ("SGM"), KPC Healthcare Holdings, Inc., KPC Health Plan Holdings, Inc., KPC Healthcare, Inc., and KPC Global Management, LLC (the foregoing also doing business as the KPC Group) (collectively, "Defendants").

I. INTRODUCTION

Defendants' Motion to Dismiss is based on three overarching arguments, none of which has merit.

First, Defendants argue this Court lacks jurisdiction by virtue of their pending appeals of certain orders in the bankruptcy proceeding. The Defendants' argument was previously considered, and rejected, by the Court in its Order Denying Stay (as defined below). *See* Adv. Docket Nos. 29, 35.

Second, Defendants challenge the Court's jurisdiction, claiming that the Adversary Proceeding is a "non-core" matter and that the non-SGM Defendants have not consented to jurisdiction of the Bankruptcy Court. Again, Defendants are incorrect. Defendants expressly consented to this Court jurisdiction and waived any right to contest such jurisdiction. The claims in the Adversary Proceeding are indisputably "core" matters that could not exist independently of the bankruptcy cases, as the underlying asset purchase agreement (the "APA") and corresponding breach arose in the bankruptcy cases. Further, the claims are core because, among other reasons, they are directly and inextricably intertwined with the sale of estate assets—the literal administration of the bankruptcy estate.

Finally, Defendants challenge the adequacy of the Complaint on many of the same grounds raised in their *Special Motion to Strike Plaintiff's Complaint Pursuant to Cal. Civ. Proc.*

Code § 425.16 [Docket No. 39]. As explained in Plaintiffs' opposition to that motion and below, each of the claims in the Complaint is recognized under California law and properly pled.

Based on the foregoing, and for the reasons fully described below, the Debtors respectfully request that the Court deny the Motion.

II. 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.

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. On December 3, 2018, William Thomas (the General Counsel of SGM and other of the Defendants) provided a letter regarding the asserted availability of certain liquidity from Chaudhuri. 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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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 APA 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 approved the APA with certain amendments, including a revised Section 8.6 [Docket 1572, Docket 2306]. *See* RJN, Ex. B and Ex. E. Specifically, the parties heavily negotiated Section 8.6 that addressed, among other things, the Debtors' ability to obtain a supplemental sale order in the event that the California Attorney General (the "Attorney General") imposed certain "Additional Conditions" therein.

5. On May 2, 2019, the Court entered an order approving the sale[1] to SGM (the "Sale Order") [Docket No. 2305-1]. *See* RJN, Ex. C. 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." *See* RJN, Ex. GG (Compl., ¶ 55).

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

B. Attorney General Review and the AG Conditions Motion

8. One of the conditions to closing under the APA was (i) the approval by 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

[1] There was no "Qualified Full Bid" for all four Hospitals, accordingly no auction was held and the Debtors declared SGM as the "winning bidder." See Docket No. 2053.

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).

9. 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).

10. 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.

11. 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 (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.

C. The AG Conditions Order

12. 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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

proposed order granting the AG Conditions Motion (the "Proposed Order"). *See id.* Despite their efforts, SGM ultimately was not a party to the Stipulation; however, after careful consideration, the Debtors and their constituents 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.*

13. 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. Proposed Order at 3; APA § 8.6 at 33.

14. 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 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.

15. 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.

16. 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.

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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

17. 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.

18. With respect to California Department of Health Care Services ("DHCS"), Plaintiffs obtained an Order [Docket No. 3372] from the 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 Court approved. [Docket Nos. 3786 & 3787.] *See* RJN, Exs. R and S.

E. The Scheduling Order

19. 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* 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.

20. 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:

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

> 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 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.

21. 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.

22. 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 efforts to render the Supplemental Sale Order a final, non-appealable order." *See* 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

23. 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.

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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.

24. 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.

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

G. Termination of the APA

26. 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 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

27. 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.

28. The Court has set a 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.

29. 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. LEGAL STANDARDS

A motion to dismiss is disfavored, and dismissal is proper only in "extraordinary cases." *United States v. White*, 893 F. Supp. 1423, 1428 (C.D. Cal. 1995) (citing *United States v. Redwood City*, 640 F.2d 963 (9th Cir.1981)); *Broam v. Bogan*, 320 F.3d 1023, 1028 (9th Cir. 2003). In resolving a Rule 12(b)(6) motion to dismiss, the Court "must accept as true all factual allegations in the complaint and draw all reasonable inferences in favor of the nonmoving party." *Retail Prop. Tr. v. United Bhd. of Carpenters & Joiners of Am.,* 768 F.3d 938, 945 (9th Cir. 2014). Further, "courts must consider the complaint in its entirety, as well as other sources courts ordinarily examine when ruling on Rule 12(b)(6) motions to dismiss, in particular, documents incorporated into the complaint by reference, and matters of which a court may take judicial notice." *Telltabs, Inc. v. Makor Issues & Rights, Ltd.,* 551 U.S. 308, 322, 127 S. Ct. 2499, 2509, 168 L. Ed. 2d 179 (2007). Not only should the complaint be construed generously, but the

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

plaintiff's brief may be used to clarify allegations in the complaint whose meaning is unclear. *See Pegram v. Herdrich*, 530 U.S. 211, 230, 120 S. Ct. 2143, 2155 fn. 10 (2000); *Orion Tire Corp. v. Goodyear Tire & Rubber Co.*, 268 F.3d 1133, 1138 (9th Cir. 2001).

Dismissal "is appropriate only where the complaint lacks a cognizable legal theory or sufficient facts to support a cognizable legal theory." *Mendiondo v. Centinela Hosp. Ctr.,* 521 F.3d 1097, 1104 (9th Cir. 2008). The motion should be denied if the complaint contains "enough facts to state a claim to relief that is plausible on its face." *Bell Atl. Corp. v. Twombly,* 550 U.S. 544, 570, 127 S. Ct. 1955, 167 L. Ed.2d 929 (2007). "A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Ashcroft v. Iqbal,* 556 U.S. 662, 678, 129 S. Ct. 1937, 173 L.Ed.2d 868 (2009). A complaint may be dismissed under Rule 12(b)(6) based on an affirmative defense "only if the defendant shows some obvious bar to securing relief on the face of the complaint." *ASARCO, LLC v. Union Pacific R. Co.*, 765 F.3d 999, 1004 (9th Cir. 2014). "If, from the allegations of the complaint as well as any judicially noticeable materials, an asserted defense raises disputed issues of fact, dismissal under Rule 12(b)(6) is improper." *Id.* (citing *Scott v. Kuhlmann*, 746 F.2d 1377, 1378 (9th Cir.1984)). If dismissal is granted under Rule 12(b)(6), leave to amend should be allowed unless the pleading may not possibly be cured by the allegation of other facts. *See Lopez v. Smith*, 203 F.3d 1122, 1130 (9th Cir. 2000).

The legal standard that applies to motions to dismiss under Rule 12(b)(1) where, as here, a defendant brings a facial challenge to the court's subject-matter jurisdiction based on the allegations in the Complaint, "the court conducts an inquiry that is 'analogous to a 12(b)(6) motion.'" *Gen. Motors Corp. v. Manly Oldsmobile-GMC, Inc.*, No. C-07-0233 JCS, 2007 WL 776261, at *2 (N.D. Cal. Mar. 12, 2007) (quoting *Roberts v. Corrothers*, 812 F.2d 1173, 1178 (9th Cir. 1987)). Accordingly, the court must consider the allegations in the complaint as true and draw all reasonable inferences in favor of the plaintiff. *See id.* A complaint should only be dismissed for lack of subject matter jurisdiction where it is clear that plaintiff will be unable to prove any set of facts which would entitle him to recover. *See id.*

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

IV. ARGUMENT

A. SGM's Appeals Did Not Divest This Court Of Jurisdiction Over This Adversary Proceeding

The Defendants inappropriately restate the divestiture argument previously put forward by SGM and rejected by this Court. The Defendants' brief divestiture argument rehashes arguments advanced by SGM, on behalf of the Defendants, in its Stay Motion. *Compare* Stay Mot. at 8 ("this Court may not take any action on Plaintiffs' Adversary Complaint, because it covers the same ground as the matters pending appeal") *with* Mot. at 10 ("Plaintiffs have not shown, because they cannot show, that the issues involved in the appeal are "separate from or collateral to" the Adversary Proceedings."). The Court rejected SGM's divestiture arguments in the Order Denying Stay. *See* RJN, Exs. KK and JJ, Adv. Docket Nos. 29, 35. Where, as here, a motion raises arguments previously considered and denied by the Court, the movant is obligated to, among other things, submit a certified statement of counsel identifying changed facts or law with respect the previously denied relief. *See* LBR 9013-1(*l*). Indeed, the Defendants cannot comply with LBR 9013-1(*l*), given that the divestiture argument is a restatement of that in the Stay Motion and is not based on new facts or law. *See id.* (requiring that the certification include, among other things, "[t]he new or different facts and circumstances claimed to exist […] and […] [t]he new or different law or legal precedent claimed to exist, which either did not exist or were not shown upon the prior motion"). As an initial matter, the Court should disregard the Defendants' divestiture argument for failure to comply with the Local Bankruptcy Rules.

SGM's divestiture argument is substantively disingenuous in light of its appeal of the Order Denying Stay. Here, the divestiture rule only divests the Bankruptcy Court of "its control over those aspects of the case involved in the appeal." *Griggs v. Provident Consumer Discount Co.*, 459 U.S. 56, 58 (1982). As a prudential rule, divestiture is flexible and "may be applied in a 'less stern' manner than true jurisdictional rules." *Rodriguez v. County of Los Angeles*, 891 F.3d 776, 790 (9th Cir. 2018). Importantly, an order subject to appeal may not be altered or expanded while subject to an appeal. *See In re Padilla*, 222 F.3d 1184, 1190 (9th Cir. 2000) ("Absent a stay or supersedeas, the trial court also retains jurisdiction to implement or enforce the judgment

or order but may not alter or expand upon the judgment."). Consequently, SGM's appeal filed on February 28, 2020 [Adv. Docket No. 50] divests this Court of jurisdiction to grant the precise divestiture relief sought by the Defendants—alteration of the Order Denying Stay. *Compare* Mot. at 10 (requesting an order dismissing the Adversary Proceeding because the "Appeals divest this Court of jurisdiction over the Adversary Proceeding") *with* Adv. Docket No. 29 (ruling that "SGM's appeals of the Orders has not divested this Court of jurisdiction over the separate issues arising in the Complaint"). Accordingly, under the Defendants' own theory, the Court does not have jurisdiction to alter its ruling finding that divestiture does not apply to the Adversary Proceeding.

Further, the Defendants' divestiture argument is substantively meritless even assuming, *arguendo*, that it may be considered by the Court while the Order Denying Stay is on appeal. As an initial matter, the Defendants submit no support for their now-contradictory assertion that the divestiture rule requires ***dismissal*** of an action rather than a ***stay*** pending resolution of the appeal. Indeed, Defendants cite to FRCP 12(b)(1), concerning subject matter jurisdiction, notwithstanding previously-cited Supreme Court precedent that confirms the divestiture rule is ***not*** jurisdictional. *See Hamer v. Neighborhood Hous. Servs. of Chicago*, 138 S. Ct. 13, 17, 199 L. Ed. 2d 249 (2017) (finding that the prudential divestiture doctrine is a "mandatory claim-processing rule," rather than jurisdictional, and admonishing that "prevailing precedent makes the distinction critical"). Additionally, under the pragmatic approach to the divestiture rule, as set forth in prior briefing and the Order Denying Stay,[2] the divestiture does not apply to the Adversary Proceeding as contended by the Defendants for at least four reasons: (i) the Court may enforce and implement the Orders because they are unstayed; (ii) the divestiture doctrine does not apply to unstayed interlocutory orders such as the Scheduling Order and MAE Order; (iii) the Appeals are not subject to the divestiture rule because they are moot in light of the termination of the APA; and (iv) SGM expressly waived the application of the divestiture doctrine when it

[2] In the interest of avoiding duplicative argument, the Debtors restate the divestiture arguments previously made to, and considered by, the Court in summary fashion. The Debtors reserve all rights to submit further and additional argument on the divestiture issue if requested by the Court.

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

waived its rights to appeal the Orders in the APA. Accordingly, the Defendants' divestiture arguments should be rejected.

B. This Court Has Jurisdiction to Adjudicate This Adversary Proceeding

Further, contrary to Defendants' assertions, this Court has jurisdiction to adjudicate the Adversary Proceeding because (i) the Adversary Proceeding is a "core proceeding" under 28 U.S.C. § 157(b) as it is predicated on actions that arose in the Bankruptcy Case itself, and (ii) there is requisite consent to Bankruptcy Court jurisdiction concerning the matters raised in the Adversary Proceeding

1. The Complaint Raises "Core" Claims Arising Under the Bankruptcy Code.

Bankruptcy Courts may hear and issue final rulings regarding core proceedings (i) arising under the Bankruptcy Code, or (ii) arising in a case under the Bankruptcy Code. 28 U.S.C. § 157(b)(1). Indeed, a matter is "core" not only when it is created or determined by the Bankruptcy Code, but also when it would have no existence outside of a bankruptcy case. *In re Harris*, 590 F.3d 730, 737 (9th Cir. 2009) (citing *In re Harris Pine Mills*, 44 F.3d 1431, 1435 (9th Cir. 1995)). The Ninth Circuit held in *Harris* that, although the underlying dispute centered on a state law cause of action for breach of a settlement agreement, the relevant claim was core because the underlying settlement agreement and corresponding breach arose in the Bankruptcy Cases and could not exist independently of the Bankruptcy Cases. The same is true here.

Additionally, the Bankruptcy Court has core jurisdiction to adjudicate the Adversary Proceeding because it is predicated on allegations that the Defendants acted tortiously in connection with the bankruptcy bidding and sale process and, ultimately, breached the APA by failing to close the Bankruptcy Court-approved sale. *Cf. 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."); *Id.* at 74 ("This motion to enforce required [the bankruptcy judge] to interpret and give effect to his prior Sale Order, and was itself a core proceeding[.]"); *In re Allegheny Health Educ. & Research Found.*, 383 F.3d 169, 176 (3d Cir. 2004) ("we hold that the bankruptcy court correctly determined that the suit was a core proceeding because it required the court to interpret and give

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

effect to its previous sale orders."); *In re Gawker Media LLC*, 581 B.R. 754, 760 (Bankr. S.D.N.Y. 2017) ("Finally, the jurisdiction is core, because the sale itself was a core proceeding, 28 U.S.C. § 157(b)(2)(N), and the '[e]nforcement and interpretation of orders issued in core proceedings are also considered core proceedings within the bankruptcy court's jurisdiction.'") (citations omitted).

None of the events set forth in the Complaint would exist but for the Bankruptcy Cases, specifically the § 363 sale order. Thus, the claims are directly and "inextricably intertwined with the sale of estate assets—the literal administration of the bankruptcy estate." *Harris*, 590 F.3d at 739. Moreover, the Bankruptcy Court approved the Sale and APA pursuant to § 363, and, as a result, "arose in" the Bankruptcy Cases under 28 U.S.C. § 157(b)(1). Any dispute concerning the interpretation of the APA is, therefore, core and subject to the Bankruptcy Court adjudication. *See* 28 U.S.C. § 157(b)(1); *see also Hawaiian Airlines, Inc. v. Mesa Air Group, Inc.*, 355 B.R. 214, 224-226 (D. Haw. 2006).

The recent Third Circuit decision in *In re Somerset Regional Water Resources, LCC*, 949 F.3d. 837, No. 19-1874, 2020 WL 628542 (3d Cir. Feb. 11, 2020) (the "S*omerset* Decision") regarding core v. non-core jurisdiction is also instructive. In the *Somerset* Decision, which is marked as "PRECEDENTIAL," the Third Circuit held that the bankruptcy court had "core" subject matter jurisdiction to enter a final order against a nondebtor third-party by virtue of its participation in the relevant bankruptcy case. *Somerset* arose out of a $1 million postpetition loan to the debtor by a lender supported by collateral, in the form of tax refunds, pledged by the debtor's owner Mr. Mostoller. After the case converted to Chapter 7, Mr. Mostoller sought the refunds for himself. The bankruptcy court ruled against Mr. Mostoller, and the decision was affirmed on appeal by the District Court and then the Third Circuit. In reaching its decision, the Third Circuit addressed a threshold issue of whether the bankruptcy court had subject matter jurisdiction to enter a final order. Somerset Decision at 9 ("Unless the parties consent, bankruptcy courts have jurisdiction to enter final judgments only in 'core proceedings.'") (citing 28 USC § 157(b), (c), *Stern v. Marshall*, 564 U.S. 462, 473-74, 482 (2011) ("*Stern*") and *Wellness Int'l Network, Ltd. v. Sharif*, 575 U.S. 665, 135 S. Ct. 1932, 1949 (2015). The Third Circuit found the

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

matter was core under 28 U.S.C.§ 157(b)(2)(D) and "because this dispute could have arisen only in bankruptcy, the bankruptcy court's exercise of jurisdiction did not offend Article III." Somerset Decision at 10. For the reasons stated above, the Somerset Decision supports the Debtors' position on the issues of this Court's core jurisdiction. Further, *Somerset* also addresses the issue of Defendants consent (as noted below), and it detracts from the Defendants' calls for a broad application of *Stern*.

2. The Parties Expressly Consented to Bankruptcy Court Jurisdiction and Waived Any Right to Contest Such Jurisdiction.

Consent to bankruptcy court jurisdiction may occur expressly or by conduct. *See Wellness Int'l Network, Ltd. v. Sharif*, 575 U.S. 665, 135 S. Ct. 1932, 1948 (2015) (consent to bankruptcy court adjudication of non-core claims may be express or implied). Here, the parties both expressly and impliedly consented to Bankruptcy Court jurisdiction over the claims raised in the Adversary Proceeding.

SGM expressly consented to exclusive Bankruptcy Court jurisdiction for the determination of "any matters arising under the" APA. RJN, Ex. C, APA § 12.3 at 41 (quoted supra at Section II.B.). A party's knowing and voluntary consent to final adjudication of issues by a bankruptcy court is enforceable even if the claims raised are non-core. *See, e.g., Wellness Int'l Network, Ltd*., 135 S. Ct. at 1949 ("The Court holds that Article III permits bankruptcy courts to decide Stern claims submitted to them by consent."). A litigant need not expressly consent to bankruptcy court jurisdiction to demonstrate consent for purposes 28 U.S.C. § 157. *See id.* at 1947 ("Nothing in the Constitution requires that consent to adjudication by a bankruptcy court be express."). However, express consent will, without question, grant the bankruptcy court final adjudicatory authority over non-core claims. *See In re Zuercher Trust of 1999*, No. 14-1372, 2016 WL 3753162, at *2 n.3 (B.A.P. 9th Cir. July 7, 2016) ("[T]here is no question here that the bankruptcy court will have authority to enter a final judgment in the underlying adversary proceeding because both parties expressly consented to the bankruptcy court entering a final judgment in this matter."); *In re Willett*, No. 15-01001, 2015 WL 8975218, at *4 (Bankr. C.D. Cal. Dec. 14, 2015) ("To the extent that the claims that form the basis of

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Mosher's Complaint and Mouderres' counterclaim are either non-core or constitute 'Stern claims,' Mosher, Willett and Mouderres expressly consent to the entry of a final judgment by the bankruptcy court.") (Bankr. C.D. Cal. Dec. 14, 2015); *accord In re Newton Enters.*, No. 14-1127, 2015 WL 3524603, at *2 (Bankr. C.D. Cal. June 3, 2015).

Despite its admission that the Adversary Proceeding relates to the Debtors' claims arising under the APA, *see* Mot. at 19-20, SGM purposefully fails to reference the APA's jurisdictional consent language or distinguish its scope concerning "any matters arising under or in connection with the" APA. RJN Ex. C, APA § 12.3 at 41.

3. The Actions of the Defendants in the Bankruptcy Case Further Support Bankruptcy Jurisdiction.

Consent is evidenced further by Defendants' participation in the Sale and related Court proceedings. Although SGM sought to shelter and otherwise minimize the participation of the Co-Defendants, the record demonstrates that all Defendants participated in the improper conduct the Debtors seek to address. Accordingly, the alter ego Defendants are directly implicated in core claims raised in the litigation. *See Northwest Territorial Mint, LLC v. Calvert (In re Northwest Territorial Mint, LLC)*, No. 16-01895, 2017 WL 568821, at *3 (W.D. Wash. Feb. 13, 2017) ("Defendant asks the bankruptcy court to determine that Plaintiff is the alter-ego of Mint. [. . .] This is a core proceeding because it goes directly to identifying property of the estate, which is key to administering it."); *see also In re Don's Making Money, LLP*, 2007 WL 1302748, at *6 (D. AZ. May 1, 2007) ("it is possible that Plaintiff's alter ego/piercing the corporate veil claim is a core claim as well"); *In re Buildings by Jamie, Inc.*, 230 B.R. 36, 44 (Bankr. D.N.J. 1998) ("The Second Circuit has held that alter ego claims to recover property of the estate are core proceedings.") (citing *St. Paul Fire and Marine Ins. Co. v. PepsiCo, Inc*., 884 F.2d 668, 701 (2d Cir. 1989)).

While discovery in the Adversary Proceeding will reveal the full extent of Defendants' alter ego status, the allegations asserted in the Complaint establish that the Co-Defendants are alter egos of SGM and that they participated in the sale process as follows:

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

- 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;
- 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.*, Ex. GG 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. 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. v. United States*, 321 F. Supp. 3d 1157, 1178 (C.D. Cal. 2018) (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. v.*

Morgan Creek Prods., Inc., 217 Cal. App. 4th 1096 (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).

Moreover, SGM's repeated efforts to raise claims and arguments on behalf of the Co-Defendants in this and other motions adds further support to the alter ego theory. A dispute as to the alter-ego status of the Co-Defendants goes directly toward identifying property of the estate, as funds flowing from the liabilities of the Co-Defendants stand to become estate assets, depending on the outcome of the Adversary Proceeding. As such, any dispute as to the alter-ego status of the Co-Defendants belongs under the purview of the Bankruptcy Court.

C. Plaintiffs' Claims For Relief Are Valid And Well Pled.

In addition to their jurisdictional arguments, Defendants repeat many of the same arguments raised in their Special Motion to Strike regarding the adequacy of Plaintiffs' allegations. As explained in Plaintiffs' Opposition to that motion, Defendants' arguments lack merit. Each of Plaintiffs' claims for relief is recognized under California law and well pled.

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

First, 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 a multitude of 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 ("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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

> 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 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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

free and clear of any interests asserted by DHCS. 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")." Finally, 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 the *Order (A) Authorizing The Sale Of Certain Of The Debtors' Assets To Strategic Global Management, Inc. Free And Clear Of Liens, Claims, Encumbrances, And Other Interests; (B) Approving The Assumption And Assignment Of An Unexpired Lease Related Thereto; And (C) Granting Related Relief* [Docket No. 2306] (the "Sale Order"). 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.

RJN, Ex. Q.

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 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." 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. Accordingly, 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,

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Ex. A, § 1.3.)[3] 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. The settlement agreement provides as follows in Paragraph 2.8:

> The Department further agrees that the payments to be made pursuant to Section 2.1 above are in full satisfaction, discharge and release of any and all claims against the Debtors, and the Hospitals or SGM arising under or related to (a) the Medi-Cal Program, including without limitation all Medi-Cal Claims and the HQA Fee claims, and (b) the California False Claims Act, and related statutes, in each case for all for goods or services, and otherwise for actions or related to periods, on or before the Medi-Cal Transfer Effective Date, *whether such claims are known or unknown*, liquidated, or contingent (the "Settlement Release").

RJN, Ex. R, Docket No. 3786, p. 16 [emphasis added].

In sum, Defendants cannot block this Adversary Proceeding by asserting that Plaintiffs never satisfied 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 and fraudulent conduct.

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

Defendants next assert that Plaintiffs' promissory fraud claim is barred by the litigation privilege and insufficiently pled. Again, they are incorrect.

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

[3] Plaintiffs' letter advising that the transaction should close by December 5, 2019 was sent as a courtesy. It was not required by the APA.

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

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.

The litigation privilege applies to statements: "(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 v. City & County of San Francisco,* 5 Cal. App. 5th, 1154 at 1162 (*citing Silberg v. Anderson,* 50 Cal. 3d 205, 212 (1990)). Here, unlike the cases they cite,[4] Defendants' false promises were 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. 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*).

[4] 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.

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

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." 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) ("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).

Accordingly, the litigation privilege has no application to the promissory fraud claim.

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." (Opp., 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. RJN, Ex. GG (Compl. Preliminary Statement, ¶¶ 102, 107, 110.) The

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

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' 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 likelihood of prevailing on their fraud claim[5] under the applicable Rule 12(b)(6) standard.

[5] In a footnote consisting only of string-cited inapplicable cases, Defendants argue that Plaintiffs' promissory fraud claim is barred by the economic loss rule. However, Defendants fail to inform the Court that there is "a split between federal district courts" in California regarding "the application of the economic loss doctrine to claims of promissory fraud[.]" *Pac. Contours Corp. v. Fives Machining Sys., Inc.*, No. SACV1800413DOCJDEX, 2018 WL 6204579, at *7–8 (C.D. Cal. Oct. 29, 2018), *report and recommendation adopted*, No. 818CV00413DOCJDEX, 2018 WL 6198461 (C.D. Cal. Nov. 28, 2018) (specifically distinguishing *JMP Sec. LLP v. Altair Nanotechnologies Inc.*, 880 F. Supp. 2d 1029, 1042 (N.D. Cal. 2012)). This Court should follow the later cases "that did not apply the economic loss doctrine to bar claims for promissory fraud," where, as here "Plaintiffs' promissory fraud claim is adequately pled." *Id.* (quotations omitted);

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

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

Defendants next assert the third claim for relief is not cognizable under California law. Not so.[6] 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

---

SVGRP LLC v. Sowell Fin. Servs., LLC, No. 16-CV-07302-VKD, 2019 WL 652890, at *13 (N.D. Cal. Feb. 15, 2019). Further, Defendants' cited cases are factually inapposite. In *De Nora Water Tech., Inc. v. Nesicolaci*, No. CV 16-9470-DMG (ASX), 2017 WL 8110006, at *3 (C.D. Cal. Aug. 2, 2017), and unlike here, counterclaimants did not "point to conduct independent of [counterclaim-defendant's] alleged breach of contract." The same is true for *JMP Sec. LLP v. Altair Nanotechnologies Inc.*, 880 F. Supp. 2d 1029, 1044 (N.D. Cal. 2012) (fraudulent misrepresentations were also alleged to be actual stand-alone contract); *Darbeevision, Inc. v. C&A Mktg., Inc.*, No. SACV1800725AGSSX, 2018 WL 5880618, at *2 (C.D. Cal. Aug. 30, 2018) (false promises were "identical to C&A's duties under the contract"); and *Grand Fabrics Int'l Ltd. v. Melrose Textile, Inc.*, No. 18-748 DSF (AFMX), 2018 WL 5880175, at *3 (C.D. Cal. Aug. 6, 2018) (same). Here, Plaintiffs' promissory fraud claim is adequately pled, and it involves fraudulent inducement of the APA, as well as fraudulent misrepresentations independent from Defendants' contractual breaches. The economic loss rule does not apply.

[6] Numerous courts have recognized the existence of such a claim outside the insurance context. *See 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); *Bullard v. Wastequip, Inc.*, 2014 WL 10987394, at *8 (C.D. Cal. Sept. 11, 2014); *Foley v. Aintabi*, 2013 WL 12130015, at *6 (C.D. Cal. Nov. 6, 2013); *Fortune Mfg. Co. v. Zurn Indus., LLC*, 2011 WL 13218043, at *3 (C.D. Cal. Aug. 31, 2011); *Unique Functional Prod., Inc. v. JCA Corp.*, 2011 WL 13355975, at *6 (S.D. Cal. May 4, 2011); *Gentec Enterprises Inc v. Transistor Devices Inc*, No. CV 10-7057 GAF (SHX), 2011 WL 13217566, at *3 (C.D. Cal. Jan. 31, 2011); *Velocity Staffing Corp., Inc. v. Resolve Staffing, Inc.*, 2008 WL 11342746, at *3 (C.D. Cal. June 16, 2008); *Rejects Skate Magazine, Inc. v. Acutrack, Inc.*, 2006 WL 2458759, at *5 (N.D. Cal. Aug. 22, 2006); *StreamCast Networks, Inc. v. IBIS LLC*, 2006 WL 5720345, at *10 (C.D. Cal. May 2, 2006); *El Dorado Irrigation Dist. v. Traylor Bros.*, 2006 WL 306914, at *5 (E.D. Cal. Feb. 7, 2006); *Putnam v. Putnam Lovell Grp. NBF Sec., Inc., a Delaware corporation*, No. C 05-1330 CW, 2005 WL 2463951, at *9 (N.D. Cal. Oct. 5, 2005); *Bea v. Sw. Airlines Co.*, No. 2005 WL 646074, at *4 (N.D. Cal. Mar. 17, 2005); *Robinson Helicopter Co. v. Dana Corp.*, 34 Cal. 4th 979, 990 (2004); *Erlich v. Menezes*, 21 Cal. 4th 543, 981 P.2d 978 (1999).

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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 will be lied to." *Id.* at 990–93 (quotations omitted). Accordingly, 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.

Moreover, 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[.]").

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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 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.

Accordingly, 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.[7]

[7] 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.

D. Plaintiffs' Alter Ego And Agency Allegations Are More Than Sufficient.

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

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. *See 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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Defendants' cited case, *Lynch v. McDonald*, 155 Cal. 704 (1909), [8] because it "merely [held] that 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.[9]

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

[8] 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 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.

[9] Moreover, *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.

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

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 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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

the affiliated companies operated, and that they all participated in the Sale process. *See supra,* pp. 17-18. 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,

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Plaintiffs have essentially been forced to lump the Bosch companies because the Bosch Defendants have chosen to operate a specific way[.]").[10]

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. It does not constitute any "concession" by Plaintiffs.

3. Plaintiffs' Agency And Conspiracy Claims Are Sufficient, As Well

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 employees cannot conspire with themselves, finding "the allegations adequately identify and link each defendant, including Merritt, to the underlying tort

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300

[10] The Court has only to read Defendants' case law, purportedly in support of Defendants' contention that Plaintiffs' alter ego allegations are insufficient, to see that it is wholly inapposite and/or misrepresented. In addition to being non-precedential New York cases, *In re Currency Conversion Fee Antitrust Litig.* and *Kingdom 5-KR-41, Ltd. v. Star Cruises PLC* are nothing like this case. In *Currency Conversion*, the complaint only alleged that a holding company "exercised such dominion and control over its subsidiaries ... that it is liable according to the law for the acts of such subsidiaries under the facts alleged in this Complaint." *See* 265 F. Supp. 2d 385, 426 (S.D.N.Y. 2003). Likewise, in *Kingdom*, the complaint only alleged "upon information and belief Star and Arrasas controlled the actions of NCL." *See* No. 01 CIV. 2946 (AGS), 2002 WL 432390, at *11 (S.D.N.Y. Mar. 20, 2002). The same is true for: (a) *McDonald v. Kiloo ApS*, 385 F. Supp. 3d 1022, 1040 (N.D. Cal. 2019), wherein the complaint used the term "Flurry" to include three entities but did not allege any other "factual basis is . . . for disregarding these entities' separate corporate forms in this manner"; (b) *In re Resistors Antitrust Litig.*, No. 15-CV-03820-JD, 2017 WL 3895706, at *4 (N.D. Cal. Sept. 5, 2017), wherein "the complaint here does not contain the kinds of express, additional allegations that this and other courts have required before accepting allegations that are made on a corporate family basis as being enough to state a claim against a subsidiary member of the family"; and (c) *Gibson Guitar Corp. v. Viacom Int'l Inc.*, No. CV 12-10870 DDP AJWX, 2013 WL 877967, at *3 (C.D. Cal. Mar. 8, 2013), wherein the court found "it does not appear plausible to the court that the role of each Defendant in the allegations would be identical" but all allegations were joint. As discussed above, only by deliberately ignoring the more-than-100 detailed factual allegations in the Complaint could Defendants assert that any of them are "insufficient" as a matter of law.

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).

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)). At the pleading stage, there is no basis to strike such claims for relief.

V. RESERVATION OF RIGHTS

This Opposition relates solely to the Defendants' request to dismiss the Complaint as set forth in the Motion. 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.

VI. CONCLUSION

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

DENTONS US LLP
601 South Figueroa Street, Suite 2500
Los Angeles, California 90017-5704
(213) 623-9300

Dated: March 4, 2020

DENTONS US LLP
SAMUEL R. MAIZEL
SONIA R. MARTIN
TANIA M. MOYRON
NICHOLAS A. KOFFROTH

By */s/ Tania M. Moyron*
Tania M. Moyron

Attorneys for Verity Health Systems of California, Inc., *et al.*

DENTONS US LLP
601 SOUTH FIGUEROA STREET, SUITE 2500
LOS ANGELES, CALIFORNIA 90017-5704
(213) 623-9300