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

KEVIN D. RISING (SBN 211633)
kevin.rising@btlaw.com
L. RACHEL LERMAN (SBN 193080)
rachel.lerman@btlaw.com
JOEL R. MEYER (SBN 247620)
joel.meyer@btlaw.com
BARNES & THORNBURG LLP
2029 Century Park East, Suite 300
Los Angeles, California 90067
Telephone: (310) 284-3880
Facsimile: (310) 284-3894

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

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA – WESTERN DIVISION

VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*, Debtors and Debtors In Possession.	Case No. 2:20-CV-00613-DSF Related to District Court Appeals: Case Nos. 2:19-cv-10352-DSF; 2:19-cv-10354-DSF; and 2:19-cv-10356-DSF
☐ 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	Lead Chapter 11 Bankr. 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;

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 Dialysis, LLC,

Debtors and Debtors-in-Possession.

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

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;

Adv. Case No. 2:20-ap-0100-ER

COUNTER-PLAINTIFF STRATEGIC GLOBAL MANAGEMENT, INC.'S OPPOSITION TO DEBTORS' MOTION TO DISMISS SGM'S AMENDED COUNTERCLAIMS, OR TO STRIKE PORTIONS THEREOF

Date: October 5, 2020
Time: 1:30 p.m.
Place: Courtroom 7D
350 West 1st Street
Los Angeles, CA 90012

Judge: Hon. Dale S. Fischer

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.

STRATEGIC GLOBAL MANAGEMENT, INC., a California corporation,

Counter-Plaintiff,

v.

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,

Debtors.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Other Authorities

I. INTRODUCTION

Debtors' Motion to Dismiss virtually ignores SGM's breach of contract arguments and focuses on return of the $30 million deposit submitted by SGM when it entered the APA. Debtors assert that SGM's claim for recovery of the deposit should be rejected because they can keep the deposit after breaching the APA and wrongfully terminating it. This argument makes no sense, and is contrary to the terms of the APA and California law.

The APA plainly states that the deposit must be returned if Debtors "commit any material default" under the Agreement. APA § 11.2. There is nothing unusual about this provision. California law mandates the return of a buyer's deposit when the seller breaches. Even if there were any ambiguity in the language of the APA, that would not be susceptible of resolution at the pleading stage.

Debtors offer an affirmative defense that is no more persuasive, namely, that the bankruptcy court precluded them from returning SGM's deposit. Debtors do not provide any support for this unidentified affirmative defense because there is none. The California Court of Appeal has expressly held that a party may not rely on a court order as a basis to breach its contractual obligations. *Webster v. Southern California First National Bank*, 68 Cal.App.3d 407 (1977).

Furthermore, SGM's claims are not based solely on Debtors' failure to return SGM's $30 million. SGM alleges a number of breaches related to Debtors' wrongful termination of the APA. These include Debtors':

- wrongful demand that SGM close the transaction based on Debtors' knowingly false representation that all closing conditions had been satisfied (First Amended Counter Claims (FACC) ¶¶ 58, 64, and 68);
- failure to satisfy the conditions of APA § 8.6 and false representation that they had done so (*id.* ¶¶ 58, 64, and 68);
- failure to properly satisfy the conditions of APA § 8.7 with respect to the Medicare and Medi-Cal provider agreement transfers, and false

representation that they had done so (*id.* ¶¶ 58, 64, and 68);

- wrongful termination of the APA despite their own knowing failure to satisfy their obligations and preconditions under the APA (*id.* ¶ 68);
- failure to comply with legal requirements applicable to the conduct and operation of the hospitals (*id.* ¶¶ 58 and 64);
- failure to obtain the approval of the Office of Statewide Health Planning and Development for the operation of several hospital facilities (*id.* ¶¶ 58 and 64);
- failure to respond to building and safety code violations and seismic compliance at St. Vincent and Seton hospitals (*id.* ¶¶ 58 and 64);
- violation of other specifically enumerated regulatory issues as set forth in the parties' correspondence (*id.* ¶¶ 58 and 64);
- allowing and precipitating the substantial and material deterioration of the net patient revenue of the hospitals in violation of APA § 4.6 (*id.* ¶¶ 23; 58; and 64);
- allowing and precipitating the substantial and material impairment of accounts receivable in violation of APA § 4.6 (*id.* ¶¶ 23; 58; and 64);
- failure to reserve funds for their accrued obligations to Independent Practice Associations, Health Plans and "Downstream Providers" (*id.* ¶¶ 58 and 64);
- belated entry into a "settlement" with the Department of Health Care Services that attempted to shift responsibility for Debtors' outstanding liabilities to SGM in violation of the APA (*id.* ¶ 68);
- false representation that Debtors would enter into an appropriate settlement agreement with DHCS (*id.* ¶ 68); and
- incurring of post-petition liability without accounting for it to SGM in violation of APA § 4.6 (*id.* ¶¶ 23; 58 and 64).

Debtors' perfunctory arguments that SGM has failed to state claims for

breach should be rejected.

II. FACTUAL BACKGROUND[1]

A. The Asset Purchase Agreement (APA)

Verity owned and operated four failing hospitals: St. Francis Medical Center, St. Vincent Medical Center, Seton Hospital, and Seton Medical Center. FACC, ¶ 1. In 2018, Verity filed for Chapter 11 bankruptcy and sought a buyer for the hospitals and related assets. *Id.*

In 2019, SGM offered to buy substantially all of the assets of the four hospitals for $610 million, subject to certain adjustments, via a stalking horse bid. *Id.* ¶ 2. Pursuant to this offer, the parties entered into the APA. *Id*.

The APA was subject to a number of conditions that Debtors needed to satisfy before SGM became obligated to close the sale, including: (1) the Attorney General's (AG's) approval of the sale without conditions that SGM had not agreed to accept (*id.* ¶¶ 25-26; APA § 8.6); and (2) Debtors' entry into settlement agreements with the Centers for Medicare and Medicaid Services and the California Department of Health Care Services that would allow the transfer of Verity's Medicare and Medi-Cal provider agreements free and clear (FACC ¶¶ 27; APA § 8.7). The APA expressly conditioned the closing on Debtors' satisfaction of these and other conditions. *See* APA § 1.3 (stating the closing date may not occur until "the satisfaction or waiver of the conditions set forth in ARTICLE 7 and ARTICLE 8."); FACC ¶ 20.

B. SGM Makes A $30 Million Good Faith Deposit.

Upon execution of the APA, SGM made a "good faith deposit" of $30 million that Debtors were permitted to hold subject to the terms and conditions of the APA. FACC ¶ 18. In entering into the APA, the parties expressly agreed that

[1] Debtors' attempt to buttress their Motion by relying on the allegations of their own First Amended Complaint (*see, e.g.* Mtn. at pp. 9-10) is improper. In ruling on Debtors' Motion, the Court should consider only the allegations of SGM's FACC and matters subject to judicial notice.

Debtors must refund SGM's deposit when, as here, they materially breached the APA. *Id*. Section 11.2 of the APA states:

> Seller Default. ***If Sellers commit any material default under this Agreement, Purchaser shall have the right to demand and receive a refund of the Deposit***, and Purchaser may, in addition thereto, pursue any rights or remedies that Purchaser may have under applicable law, including the right to sue for damages or specific performance.

By including this provision in the APA, the parties made clear their understanding that the $30 million deposit would be returned to SGM if Debtors materially breached the APA. *Id.*

In addition, under APA § 9.1, SGM also had the right to demand and immediately receive the return of its $30 million deposit if the transaction had not closed by December 31, 2019. *Id.* ¶ 29.

C. Debtors Attempt to Force A Sale without Satisfying Their Contractual Obligations.

Between January and October 2019, SGM and Debtors worked constructively towards a closing of the Sale under the APA. FACC ¶ 30. These efforts included SGM's negotiation and ultimate agreements with numerous labor unions to modify their respective collective bargaining agreements; analysis of hundreds of executory contracts to be assumed, including those with health plans, medical practice groups, independent physician associations (IPAs), vendors and suppliers; and the drafting of numerous separate agreements, such as an interim management agreement and sale-leaseback agreement, which would need to be completed and put in place at the time of closing. *Id.* SGM devoted substantial financial resources to hire consultants, attorneys, and other expert and in-house personnel to address these and numerous other issues essential to the acquisition of four financially distressed hospitals. *Id.*

By the fall of 2019, Debtors realized that they had not satisfied their

contractual obligations to SGM, *inter alia*, under APA §§ 8.6 and 8.7. *See id.* ¶¶ 32-44 (detailing Debtors' failure to satisfy their contractual obligations under APA §§ 8.6 & 8.7). With APA § 9.1's December 31, 2019 deadline looming, Debtors' failure to satisfy their obligations put them at risk that SGM would terminate the APA and demand the return of its $30 million or to renegotiate its terms. *Id.* ¶ 31. To avoid this outcome, Debtors developed and implemented a strategy to assert that SGM had breached the APA, which would give Debtors a pretext to terminate the APA, keep SGM's $30 million, and pass the blame for the sale's failure to close by December 31 on to SGM. *Id.*

On November 20, 2019, Debtors, through their counsel, sent SGM a letter falsely representing that they had satisfied all conditions to close as of November 19, 2019, and demanding that SGM close the sale by December 5, 2019 or be deemed in breach of the APA. *Id.* ¶ 45. Debtors' letter contained at least two misrepresentations with respect to their satisfaction of APA §§ 8.6 and 8.7. *Id.* First, Debtors falsely represented they had satisfied APA § 8.6 when they had not. *Id.* Second, Debtors claimed they had satisfied APA § 8.7 because: "Yesterday, as we notified you, the Debtors reached a settlement agreement with the United States, on behalf of Department of Health and Human Services [HHS] and the Centers for Medicare and Medicaid Services [CMS], allowing for the transfer of the Medicare Provider Agreement without successor liability." *Id.* Debtors' letter does not mention any settlement of their ongoing dispute with the California Department of Health Care Services [DHCS] regarding the transfer of the Debtors' Medi-Cal provider agreements to SGM and DHCS' recoupment rights. *Id.* No such settlement existed at the time. *Id.* To the contrary, DHCS and Debtors were actively litigating the issue amongst themselves. *Id.* In short, Debtors knowingly misrepresented that all conditions to close had been satisfied when they had not.

In response, SGM wrote Debtors two letters advising them of their noncompliance with their obligations under the APA. *Id.* ¶ 48. SGM's letters

explained that Debtors had failed to satisfy numerous obligations under the APA, including, but not limited to their:

- failure to comply with legal requirements applicable to the conduct and operation of its hospitals, including, but not limited to, serious and material Health and Safety Code violations;
- materially breaching APA §§ 2.8, 2.10, and 4.6;
- failure to obtain the approval of the Office of Statewide Health Planning and Development for the operation of several hospital facilities;
- failure to satisfy the conditions of APA § 8.7 with respect to the Medicare and Medi-Cal provider agreement transfers;
- failure to satisfy the conditions of APA § 8.6;
- failure to respond to building and safety code violations and seismic compliance at St. Vincent and Seton hospitals or even to obtain the funds required to do so – thereby improperly shifting the costs to SGM;
- other specifically enumerated regulatory issues;
- substantial and material deterioration of the net patient revenue of the hospitals;
- fraudulently withholding information concerning serious health and safety issues from SGM despite being legally obligated to disclose such conditions;
- substantial and material impairment of accounts receivable;
- failure to reserve and to disclose its failure to reserve for its accrued obligations to Independent Practice Associations, Health Plans and "Downstream Providers"; and
- incurrence of post-petition liability in violation of, *inter alia*, APA § 4.6(e). *Id*.

Debtors refused to address the lion's share of issues identified in SGM's letters. *Id.* ¶ 50. With respect to § 8.7, they asserted, incorrectly, that the bankruptcy

court's two prior orders regarding the sale "afford equal or greater protection to SGM than any settlement could have, thereby satisfying Section 8.7." *Id.* Neither order eliminated DHCS' recoupment rights against SGM and the assets SGM was acquiring pursuant to the APA, so they could not possibly satisfy § 8.7, even assuming arguendo that court orders could be substituted for the settlement agreement that the APA required. FACC ¶¶ 32-44; 51.

Debtors also stated, incorrectly, that a settlement with DHCS had been reached on November 22. *Id*. ¶ 50. As Debtors' counsel acknowledged at a hearing on November 26, 2019, Debtors had yet to reach a settlement agreement with DHCS meeting the requirements of § 8.7, which mandated: (1) resolution of all outstanding financial defaults under Debtors' Medi-Cal Provider Agreements, and (2) full satisfaction, discharge, and release of DHCS's claims under the Medi-Cal Provider Agreements, with respect to both Verity and SGM. *Id.* ¶ 51.

Debtors did not reach any settlement agreement with DHCS until December 9, 2019, four days *after* the date they insisted SGM must close. *Id.* ¶ 52. By then, Debtors had already breached the APA by delivering a false notice of closing on November 20, 2019 and demanding that SGM close by December 5, 2019. *Id.*

D. Debtors Wrongfully Terminate the APA and Refuse to Return SGM's $30 Million Deposit.

On December 5, 2019, SGM sent Debtors a letter notifying them that they were in material default of the APA and demanding the immediate return of its $30 million deposit, with interest, pursuant to APA § 11.2. FACC ¶ 53. Debtors refused to return the deposit. *Id.* Instead, on December 6, 2019, Debtors filed an "emergency motion for issuance of an order to show cause why SGM failed to close the sale by December 5, 2019" seeking an order finding that SGM had breached the APA. The bankruptcy court denied Debtors' motion and ruled that the parties must litigate their respective claims regarding breach of the APA, and whether Debtors must return SGM's $30 million deposit. *Id*.

On December 17, 2019, Debtors sent SGM a letter entitled "Notice of Termination Effective Date," stating that SGM had breached the APA by failing to close and terminating the APA effective December 27, 2019. FACC ¶ 54.

On January 3, 2020, Debtors filed a Notice of the Termination of the APA with the bankruptcy court. *Id.*

E. SGM's Claims Against Debtors.

SGM asserts three claims against Debtors: (1) breach of contract; (2) breach of the implied covenant of good faith and fair dealing; and (3) tortious breach of contract. FACC ¶¶ 56-71. These claims are not "premised on the allegation that the APA requires [Debtors] to refund the Deposit," as Debtors claim. Mot. at 11:1-3. Instead, SGM's claims derive from Debtors' wrongful efforts to force a close of the transaction without having satisfied their obligations under the APA, and their subsequent wrongful termination of the APA. Specifically, SGM alleges that Debtors breached the APA and the implied covenant of good faith and fair dealing by:

- wrongfully demanding that SGM close the transaction based on the knowingly false representation that all closing conditions had been satisfied (FACC ¶¶ 58, 64, and 68);
- failing to satisfy the conditions of APA § 8.6 and falsely representing that they had done so (*id.* ¶¶ 58, 64, and 68);
- failing to properly satisfy the conditions of APA § 8.7 with respect to the Medicare and Medi-Cal provider agreement transfers, and falsely representing that they had done so (*id.* ¶¶ 58, 64, and 68);
- wrongfully terminating the APA based on SGM's failure to close the transaction on or before December 5, 2019, despite their own knowing failure to satisfy their obligations and preconditions under the APA (*id.* ¶ 68);
- failing to comply with legal requirements applicable to the conduct and

operation of the hospitals (*id.* ¶¶ 58 and 64);

- failing to obtain the approval of the Office of Statewide Health Planning and Development for the operation of several hospital facilities (*id.* ¶¶ 58 and 64);
- failing to respond to building and safety code violations and seismic compliance at St. Vincent and Seton hospitals (*id.* ¶¶ 58 and 64);
- violating other specifically enumerated regulatory issues as set forth in the parties' correspondence (*id.* ¶¶ 58 and 64);
- allowing and precipitating the substantial and material deterioration of the net patient revenue of the hospitals in violation of APA § 4.6 (*id.* ¶¶ 23; 58; and 64);
- allowing and precipitating the substantial and material impairment of accounts receivable in violation of APA § 4.6 (*id.* ¶¶ 23; 58; and 64);
- failing to reserve and to disclose its failure to reserve for its accrued obligations to Independent Practice Associations, Health Plans and "Downstream Providers" (*id.* ¶¶ 58 and 64);
- belatedly entering into a "settlement" with the Department of Health Care Services without SGM's approval, which impermissibly attempted to shift responsibility for Debtors' outstanding liabilities to SGM in violation of the APA (*id.* ¶ 68);
- falsely representing to SGM that Debtors would enter into an appropriate settlement agreement with DHCS that would result in the "resolution of all outstanding financial defaults under any of [Debtors'] Medicare and Medi-Cal provider agreements" and "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 [Debtors] or [SGM] for monetary liability arising under the Medicare or Medi-Cal provider agreements" without intending to do so (*id.* ¶ 68);

- incurring post-petition liability without accounting for such to SGM in violation of APA § 4.6 (*id.* ¶¶ 23; 58 and 64); and
- wrongfully withholding SGM's $30 million dollar deposit despite Debtors' multiple material breaches of the APA and their failure to satisfy the express conditions in the APA (*id.* ¶¶ 58 and 64).

III. ARGUMENT

A. Debtors' Argument that They Can Breach the APA, Wrongfully Terminate It, and Still Keep SGM's $30 Million Deposit Is Meritless.

Debtors' Motion is premised on a flawed assumption—that SGM's $30 million deposit is non-refundable even when, as here, Debtors materially breached the APA and then wrongfully terminated it. *See* Mot. at 12:12-16:8 (erroneously claiming that SGM is only entitled to a refund if SGM first terminated the APA). Neither the APA's text nor California law supports this bizarre result.

1. The APA Unambiguously Requires Debtors to Return SGM's $30 Million "Good Faith" Deposit Should They Breach the APA.

Debtors read the APA to say that SGM's deposit is non-refundable unless SGM terminates the APA under § 9.1(d), even if Debtors breach the APA and then terminate the agreement themselves under Section 9.1(b). *See* Mot. 13:4-5; 14:6-8. These assertions ignore APA § 11.2's plain language, which addresses the situation where, as here, Debtors wrongfully breach the APA.

APA § 11.2 expressly states that "[i]f Sellers commit any material default under this Agreement, Purchaser shall have the right to demand and receive a refund of the Deposit" and to "pursue any rights or remedies that Purchaser may have under applicable law, including the right to sue for damages or specific performance."

This text is plain, unambiguous, and requires the denial of Debtors' Motion as a matter of law. "So long as the [plaintiff] does not place a clearly erroneous

construction upon the provisions of the contract, in passing upon the sufficiency of the complaint, we must accept as correct plaintiff's allegations as to the meaning of the agreement." *Rutherford Holdings, LLC v. Plaza Del Rey*, 223 Cal.App.4th 221, 229 (2014).

Debtors argue that APA § 11.2 "merely outlines the remedies in the event of a termination under Section 9.1(b) or (d)." Mot. at 14:22-26. Not so. Nothing in APA § 11.2 or its placement in the APA suggests it is so limited or impairs SGM's right to the return of its deposit if Debtors materially breach the APA. Debtors base their argument on the following partial sentence in APA § 9.2: "in the case of any termination based on Sections 9.1(b) or (d) the consequences of such termination shall be determined in accordance with ARTICLE 11 hereof." Mot. at 14:22-26. The full text of APA § 9.2, however, demonstrates that the quoted language does not nullify APA § 11.2's plain language, but merely addresses the parties' rights to recover attorneys' fees and costs in the event of termination. The full text of APA § 9.2 reads:

> 9.2 Termination Consequences. **If this Agreement is terminated pursuant to Sections 6.1(b), 6.2 or 9.1**: (a) all further obligations of the parties under this Agreement shall terminate (other than Purchaser's right to receive the Break-Up Fee if applicable), provided that the provisions of ARTICLE 12, shall survive; and (b) **each party shall pay only its own costs and expenses incurred by it in connection with this Agreement; provided, in the case of any termination based on Sections 9.1(b) or (d) the consequences of such termination shall be determined in accordance with ARTICLE 11 hereof**. In addition, if this Agreement is terminated pursuant to Sections 6.1(b), 6.2 or 9.1 (other than Section 9.1(b)), Seller shall immediately return the Deposit to Purchaser with all interest earned thereon. Each Party acknowledges that the agreements contained in this Section 9.2 are an integral part of the transactions contemplated by this Agreement, that without these agreements such Party would not have entered into this Agreement.

APA § 9.2(b) (emphasis added).

Pursuant to the above, the default position when the APA is terminated under §§ 6.1(b), 6.2, or 9.1 is that each side is responsible for its own fees and costs. Notwithstanding this default position, if SGM were to terminate the APA pursuant to the provisions cited therein, it would be entitled to its attorneys' fees, costs, punitive damages, etc. (*i.e.* "any rights and remedies that [SGM] may have under applicable law" [APA § 11.2]), "provided" that it could show that Debtors materially breached the agreement.

Debtors' interpretation would require the Court to ignore the first half of the very sentence they quote. A contract may not be interpreted in a way that renders one of its provisions meaningless. *Turlock Irrigation Dist. v. Fed. Energy Regulatory Comm'n*, 903 F.3d 862, 872 (9th Cir. 2018) ("We will not interpret a contract so as to render one of its provisions meaningless") accord, *Hemphill v. Wright Family, LLC,* 234 Cal.App.4th 911, 915 (2015) ("Courts must interpret contractual language in a manner which gives force and effect to every provision, and not in a way which renders some clauses nugatory, inoperative or meaningless.")

Debtors' argument that APA § 9.2 nullifies the plain language of § 11.2 is further belied by the fact that APA § 9.2 *itself* states that SGM's $30 million deposit must be returned in the event of a termination under APA § 9.1: "In addition, if this Agreement is terminated pursuant to Sections 6.1(b), 6.2 or 9.1 (other than Section 9.1(b)), Seller shall immediately return the Deposit to Purchaser with all interest earned thereon."

In sum, APA § 11.2 unambiguously addresses the situation facing this Court and mandates the return of SGM's $30 million deposit if this Court finds that Debtors materially breach the APA.

Debtors' argument that there is no applicable scenario in which SGM is entitled to the return of its $30 million deposit unless SGM terminates the

agreement under APA § 9.1(d) is not only contrary to the APA, it violates well-established tenets of California law.

If Debtors were correct, the APA would be illusory, because Debtors would have no obligations with respect to SGM's $30 million. Both California and federal law explicitly reject such a proposition. *Kennewick Irr. Dist. v. United States*, 880 F.2d 1018, 1032 (9th Cir. 1989) ("Preference must be given to reasonable interpretations as opposed to those that are unreasonable, or that would make the contract illusory."); *ASP Properties Group, L.P. v. Fard, Inc.* 133 Cal.App.4th 1257, 1269 (2005) ("Interpretation of a contract must be fair and reasonable, not leading to absurd conclusions. The court must avoid an interpretation which will make a contract extraordinary, harsh, unjust, or inequitable.") (internal citations omitted); *Khavarian Enterprises, Inc. v. Commline, Inc.*, 216 Cal.App.4th 310, 318 (2013) ("If a contract is capable of two constructions courts are bound to give such an interpretation as will make it lawful, operative, definite, reasonable, and capable of being carried into effect ...").

Debtors' understanding of the APA would also result in an impermissible forfeiture of SGM's $30 million. *See Greentree Fin. Grp., Inc. v. Executive Sports, Inc.*, 163 Cal. App. 4th 495, 499 (2008); *Milenbach v. Comm'r*, 318 F.3d 924, 936 (9th Cir. 2003) ("Where there are two possible interpretations of a contract, one that leads to a forfeiture and one that avoids it, California law requires the adoption of the interpretation that avoids forfeiture, if at all possible.").

2. Even If This Court Finds That the APA is Ambiguous with Respect to The Return of SGM's $30 Million Deposit, It Must Deny Debtors' Motion.

As set forth above, the plain language and only reasonable interpretation of APA § 11.2 entitles SGM to the return of its $30 million deposit here. This plain language is supported by the extrinsic evidence of the parties' intent (FACC ¶ 28), to be presented, if necessary, at trial. Debtors counter with their own contrary

interpretation. When, as here, the parties offer inconsistent interpretations of a contract, and both interpretations may be reasonable in light of extrinsic evidence, the court must review such evidence and evaluate it before admitting any evidence or reaching a decision on the correct interpretation of the contract. *Pac. Gas & Elec. Co. v. G. W. Thomas Drayage & Rigging Co.*, 69 Cal.2d 33, 39 (1968) (*Drayage*); *First Nat. Mortg. Co. v. Federal Realty Inv. Trust*, 631 F.3d 1058, 1066-67 (9th Cir. 2011) (quoting *Drayage, supra*) ("The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible.").

Contract interpretation therefore involves a two-step process by which the Court first "provisionally receives (without actually admitting) all credible evidence concerning the parties' intentions to determine 'ambiguity,' *i.e.*, whether the language is 'reasonably susceptible' to the interpretation urged by a party. If in light of the extrinsic evidence the court decides the language is 'reasonably susceptible' to the interpretation urged, the extrinsic evidence is then admitted to aid in the second step – interpreting the contract." *F.B.T. Productions, LLC v. Aftermath Records*, 621 F.3d 958, 963 (9th Cir. 2010) (quoting *Winet v. Price*, 4 Cal. App. 4th 1159 (1992)).

Accordingly, under California law, the court must resolve any ambiguity in SGM's favor at the pleading stage, and deny Debtors' Motion. *Consul Ltd. v. Solide Enters., Inc.*, 802 F.2d 1143, 1149 (9th Cir. 1986) ("Where the language leaves doubt as to the parties' intent, the motion to dismiss must be denied."); *Banc of California Nat'l Ass'n v. Fed. Ins. Co.*, 2020 WL 3655500, at *4 (C.D. Cal. Apr. 24, 2020) (at the motion to dismiss stage, "[the Court must] strive to resolve any contractual ambiguities in the [non-moving party's] favor."); *Westlands Water Dist. v. U.S. Dep't of Interior*, 850 F.Supp. 1388, 1408 (E.D. Cal. 1994) ("A motion to

dismiss cannot be granted against a complaint to enforce an ambiguous contract.").

3. Debtors' Motion Must Be Denied Because SGM Has Sustained $30 Million in Damages

SGM alleges it has suffered, at minimum, $30 million in damages as a result of Debtors' breach. When, as here, a party accepts a deposit, and then materially breaches and wrongfully terminates the underlying agreement, the lost deposit is an element of the non-breaching party's damages. *Rutherford Holdings*, 223 Cal. App. 4th at 228-29. To hold otherwise would improperly insulate Debtors from liability for fundamental breaches of the APA, including their improper termination.

B. The Bankruptcy Court's Sale Order Does Not Require Dismissal of SGM's Claims.

Debtors argue that SGM's Counterclaims must be dismissed because: (1) they are premised exclusively on Debtors' refusal to return SGM's $30 million deposit (Mot. at 11:1-2) and (2) the bankruptcy court's orders preclude them from returning the deposit (*id.* at 16:11-17:19). Both arguments are unavailing.

First, SGM's claims are not premised exclusively on Debtors' refusal to return SGM's $30 million deposit. As set forth above, SGM seeks damages based on Debtors' breaching the APA by intentionally noticing a false closing date as a pretext to wrongfully terminate the APA. *See supra* Section II, E.[2]

Second, Debtors argue that because the bankruptcy court's Sale Order required SGM's $30 million deposit to be held in an Escrow Deposit Account, they are absolved from liability for their wrongful refusal to return the deposit pursuant to the APA's terms. Debtors' argument is effectively an assertion of an unidentified affirmative defense. *Ahmed v. HSBC Bank USA, Nat'l Ass'n*, 2017 WL 5720548, at *2 (C.D. Cal. Nov. 6, 2017) ("An affirmative defense is defined as a defendant's

[2] Knowing their arguments concerning the basis of SGM's claims are meritless, Debtors alternatively ask the Court to strike any mention of their wrongful withholding of SGM's $30 million deposit from the FACC. Plaintiffs' arguments are meritless – SGM is entitled to the return of its $30 million deposit. *See supra* Sections III, A, 1-3.

assertion raising new facts and arguments that, if true, will defeat the plaintiff's claim, even if all allegations in the complaint are true."); *A.K.C. v. City of Santa Ana, No.*, 2010 WL 11469021, at *1 (C.D. Cal. July 13, 2010) (same). Debtors' Motion does not cite a single case supporting their affirmative defense because there is none. The California Court of Appeal expressly rejected an argument similar to Debtors' in *Webster v. Southern California First National Bank*. 68 Cal.App.3d 407 (1977).

Webster involved the sale of a bar with escrow handled by Southern California First National Bank (the Bank). *Id.* at 411. After escrow opened, the Bank received a letter from a creditor, Migliore, claiming he was owed money on a promissory note from the bar's seller. *Id.* at 412. Thereafter, two other creditors, Lewis and Patterson, filed a lawsuit claiming priority over the proceeds of the sale. *Id.* The court issued an injunction precluding the Bank from distributing any sale proceeds absent a court order. *Id.* Accordingly, the Bank did not distribute any funds during escrow unless the court ordered it to do so. *Id.*

After escrow closed, Migliore sued the Bank for failing to pay his claim. *Id.* at 413. In its answer, the Bank asserted the affirmative defense that it only acted as directed by the court. *Id.* The Bank sought summary judgment on this defense and argued that it "had disbursed the funds specifically as directed by the court" and that it could not have paid Migliore "without being in direct violation of court orders." *Id.* The Bank argued, "[i]t is inherently unreasonable to impose liability on the bank for doing exactly what it was ordered by this court to do." *Id.*

The Court of Appeal rejected the Bank's arguments and held that a court order or process obtained by a private litigant could not absolve the Bank of liability. *Id.* at 415. In so holding, the court noted, "It is of interest that the Bank has not supported its argument (either here or in the trial court) by a single citation of authority. While the argument has surface appeal, we find it will not withstand legal scrutiny…." *Id.* Because the Bank was a party to the injunction litigation and had

participated in stipulations that led to the orders restricting the issuance of the payments, the Bank could not argue that it was compelled by the court to act contrary to its previously undertaken duties. *Id.* at 416.

As in *Webster*, Debtors cannot rely on the bankruptcy court's Sale Order to avoid liability to SGM. Like the Bank in *Webster*, Debtors present no authority in support of any affirmative defense that would compel such a result. Instead, like the Bank, Debtors and their secured lenders were active participants in the bankruptcy case. Debtors, having consented to the Sale Order or otherwise participated in the acquiescence of the Order, cannot argue that the Order bars them from returning a deposit under the terms of the previously executed APA (which, as set forth above, clearly requires the return of SGM's deposit). Other California authorities are in accord. *See Irwindale Citrus Ass'n v. Semler*, 60 Cal.App.2d 318, 324 (1943) (A party is not excused from performance of its obligations under a contract even if a court order prevents the party from performing its obligations); *Union Contracting & Paving Co. v. Campbell*, 2 Cal.App. 534, 537 (1905) (held that the issuance of an injunction in an unrelated lawsuit, which prevented the timely performance of defendant's services for plaintiff, did not excuse the defendant of its obligations to timely perform its services for plaintiff).

C. SGM Has Alleged a Valid Claim for Breach of Contract.

After spending the vast majority of their Motion setting forth the meritless arguments above, Debtors briefly argue that SGM's breach of contract claim does not satisfy Rule 8's notice pleading standard. *See* Mot. at 19:1-2. Debtors are wrong again.

Federal Rule of Civil Procedure Rule 8(a)(2) requires only a "short and plain statement of the claim showing the pleader is entitled to relief." Fed. R. Civ. Proc. 8(a)(2). "[U]nder the relaxed pleading standards of the Federal Rules, the idea was not to keep litigants out of court but rather to keep them in. The merits of a claim would be sorted out during a flexible pretrial process and, as appropriate, through

the crucible of trial." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 575 (2007). Thus, to survive a motion to dismiss, the plaintiff need only plead "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 (2009). To state a cause of action for breach of contract, the plaintiff must allege: (1) the existence of a contract, (2) plaintiffs' performance, (3) defendants' breach, and (4) plaintiffs' resulting damages. *Careau & Co. v. Sec. Pacific Business Credit, Inc.*, 22 Cal.App.3d 1371, 1388 (1990). That is all that is required. *See, e.g. Henry v. Ocwen Loan Servicing, LLC*, 2017 WL 3669623, at *4 (S.D. Cal. Aug. 23, 2017) ("to state a breach of contract claim in federal court, the pleading need only provide the bare outlines of [a] claim consistent with the federal notice pleading framework under Fed.R.Civ.P. 8(a)."); *Wynes v. Kaiser Permanente Hosps.*, 2011 WL 1302916, at *11 (E.D. Cal. Mar. 31, 2011) ("allegations of an existence of a written contract, performance under the contract, breach of contract, causation, and damages is sufficient to meet the federal notice pleading standards.").

SGM's Counterclaims more than satisfy Rule 8(a)(2). SGM alleged the existence of a contract (FACC ¶¶ 2; 17; 56), its performance thereunder (*id.* ¶¶ 18; 30; 57), Debtors' numerous breaches (*id.* ¶¶ 3-7; 20-23; 31; 45-49; 51-55; 58-59), and SGM's resulting damages (*id.* ¶¶ 30; 60-61). That is sufficient as a matter of law.

Debtors nevertheless argue that SGM's breach of contract claim fails because it did not "link" the alleged breaches "to any specific provisions in the APA prohibiting such conduct." *See* Mot. at 18:5-6. Debtors cite no authority for this argument. SGM far exceeded Rule 8's "short and plain statement" requirement, and set forth in detail the specific provisions of the APA establishing the obligations that Debtors failed to satisfy before trying to force a sale and wrongfully terminating the APA. *See* FACC ¶¶ 20-29; 32-35; 48-49; 51-53.

SGM also alleged that Debtors breached the implied covenant of good faith

and fair dealing by "deliberately acting to deprive SGM of the benefits of the APA and by purposefully interfering in the APA such that it materially harmed SGM." FACC ¶¶ 62-66. This too is sufficient. "Breach of a specific provision of the contract is not necessary to a claim for breach of the implied covenant of good faith and fair dealing." *Thrifty Payless, Inc. v. The Americana at Brand, LLC*, 218 Cal.App.4th 1230, 1244 (2013) (citation omitted).

Finally, Debtors briefly argue that SGM's breach of contract claim fails because SGM "fails to allege that it would have closed the transaction absent the Other Alleged Breaches." Mot. at 19:10-11. Once again, Debtors do not cite any applicable authority setting forth such a requirement. Debtors cite *Hellenic Petroleum LLC v. Elbow River Mktg. Ltd.*, 2019 WL 6114892, at *1 (E.D. Cal. Nov. 18, 2019) (Mtn. at 19:15-21), but the case is inapposite and does not support Debtors' theory in any event. *Hellenic Petroleum* was not decided under California law, but the United Nations Convention on Contracts for the Internal Sale of Goods. And it made no finding that the plaintiff had to plead what it would have done in a hypothetical world where Debtors complied with their obligations.

D. SGM's Tortious Breach of Contract Claim Satisfies the Requirements Set Forth in Debtors' Own Briefs.

Debtors attempt to dismiss SGM's claim for tortious breach of contract on the grounds that SGM has not pled an "independent tort." (Mot. at 19:26-22:25). Essentially, Debtors argue that to state a claim for intentional breach of contract, a plaintiff must also allege an independent fraud claim. Debtors' claim is refuted by their own prior position in this litigation. As this Court is aware, SGM moved to dismiss Debtors' own "tortious breach" claim on the ground no such claim existed under California law. In defending their claim, Debtors stated that under the California Supreme Court's decision in *Robinson Helicopter*, a tortious breach of contract may be found in any of three circumstances: (1) when "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." ECF No. 46 at 23:15-24:5 (emphasis added).

Debtors explicitly argued that these circumstances are stated in the disjunctive, and that a party may maintain a claim for "tortious breach" under each scenario. *See id.* ("Here, the FAC alleges all three circumstances, which is more than sufficient to state a claim for relief under Rule 12(b)(6)."). Debtors reiterate this language again in their Motion. *See* Mot. at 19:27- 20:4. SGM has adequately alleged a tortious breach of contract under Debtors' theory of the tort because they have alleged Debtors breached the contract in a manner "involving deceit or undue coercion" and/or intentionally breached the APA "intending or knowing that such a breach will cause . . . substantial consequential damages."

Debtors' assertion that SGM's tortious breach of contract claim is barred by the litigation privilege also contradicts their own prior argument. Again, in Debtors' own words, "the litigation privilege does not apply to a 'tortious course of conduct,' which is precisely what is alleged in this case." ECF No. 46 at 16-24 (citing cases). Debtors cannot simply reverse course when confronted with their own arguments concerning the nature of their own claims. *Pegram v. Herdrich*, 530 U.S. 211, 228 n.8 (2000) (holding that the doctrine of judicial estoppel "prevents a party from prevailing in one phase of a case on an argument and then relying on a contradictory argument to prevail in another phase."). Moreover, even if the litigation privilege did apply (it does not), it would not bar SGM's claim for tortious breach of contract as a result of Debtors' breach of the contract using "deceit or coercion" or intentional breach of the APA "intending or knowing" that such a breach would cause SGM substantial consequential damages.

In sum, the language of SGM's tortious breach claim tracks Debtors' allegations almost verbatim. *Compare, e.g.*, FACC ¶¶ 68-71 to FAC ¶¶ 124-127.

Either SGM is correct and *Robinson Helicopter* did not create a new tort for "tortious breach of contract" (in which case both parties' claims must be dismissed), or SGM has validly pled such a claim by alleging that Debtors breached the contract in a way that "involved deceit or coercion," or that they did so "intentionally, … intending or knowing that such a breach will cause substantial damages."

IV. CONCLUSION

For the foregoing reasons, Debtors' Motion to Dismiss should be denied.

Dated: September 14, 2020

LEVENE, NEALE, BENDER, YOO & BRILL L.L.P.

By:/s/Gary E. Klausner
Gary E. Klausner

Dated: September 14, 2020

BARNES & THORNBURG LLP

By:/s/ Kevin D. Rising
Kevin D. Rising

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

SIGNATURE ATTESTATION

Pursuant to Local Rule 5-4.3.4(a)(2)(i), I, Kevin D. Rising, attest that all other signatories listed, and on whose behalf this filing is submitted, concur in the filing's content and have authorized the filing.

Dated: September 14, 2020

/s/Kevin D. Rising
Kevin D. Rising