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UNITED STATES DISTRICT COURT

FOR THE CENTRAL DISTRICT OF CALIFORNIA

WESTERN DIVISION - LOS ANGELES

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

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,

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

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

Hon. Dale S. Fischer

PLAINTIFFS' REPLY MEMORANDUM IN SUPPORT OF THEIR MOTION TO DISMISS DEFENDANT STRATEGIC GLOBAL MANAGEMENT'S AMENDED COUNTERCLAIMS

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

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,

Counter-Defendants.

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I. INTRODUCTION

SGM's Opposition confirms it cannot recover the Deposit under the Asset Purchase Agreement ("APA").[1] SGM does not dispute that Section 1.2 of the APA expressly states the Deposit is "non-refundable" unless one of four provisions of the APA is satisfied. And SGM admits that none of those provisions were satisfied. Instead, SGM asserts that a different section of the APA (Section 11.2) rendered the mandatory requirements of Section 1.2 meaningless. As a matter of controlling contract interpretation rules, SGM's position is meritless. Pursuant to Section 11.2, SGM could have recovered the Deposit if it had properly terminated the APA based on a material default by Plaintiffs. Because SGM admittedly never did so, Section 11.2 does not apply.

Nor does SGM dispute that Plaintiffs have been *under court orders* not to release the Deposit, including the current Confirmation Order (as defined below) that provides the Deposit *cannot be released* unless and until this Court enters a judgment. *See* Plaintiffs' RJN, Exs. B-H, O-S. Critically, SGM itself supplied the controlling language incorporated into the Confirmation Order, and expressly agreed to it.[2] As importantly, its assertion that a court order does not excuse contract performance is unsupported by California law. Engaging in conduct required by court order is not "wrongful." Further, SGM knew the Deposit was maintained in a segregated account that could not be released absent a court order, and yet never took any steps to ask the Court to release it, despite having every opportunity to do so. SGM cannot turn its own undisputed inaction into a basis for claims against Plaintiffs. Accordingly, SGM's claim that Plaintiffs breached the APA and its implied covenant of good faith and fair dealing by "wrongfully withholding/retaining" the Deposit should be dismissed on this additional ground. Counterclaim, ¶¶ 55, 58, 60, 64-65, 68.

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[1] Capitalized terms not otherwise defined herein shall have the definitions set forth in the Motion to Dismiss SGM's Amended Counterclaims (ECF 61).

[2] *See* Plaintiffs' RJN, Ex. N (Omnibus Reply at 6-7); *id.*, Ex. O (Disclosure Statement at 43); *id.*, Ex. P (SGM Limited Objection at 1-2); *id.*, Ex. Q (Order on SGM Limited Objection at 4).

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In addition, SGM fails to respond to Plaintiffs' argument that its conclusory smattering of other alleged APA breaches are unsupported by factual allegations and are untethered from the APA. SGM fails to identify the provisions of the APA that it contends were breached through the vague hospital operational issues referenced in the Counterclaim. Indeed, such allegations are simply not actionable, as a matter of law, given the APA's express "AS IS, WHERE IS" provision. In sum, SGM fails to adequately allege claims based on any other alleged conduct that was distinct from the alleged "wrongful[] withholding" of the Deposit.

Finally, SGM's Opposition ("Opp.") makes clear that its Third Count, for alleged tortious breach of the APA, must be dismissed. A tortious breach requires that a breach of contract be accompanied by a traditional common law tort, such as fraud or conversion. In an attempt to satisfy this requirement, SGM alleges Plaintiffs committed fraud when their attorney sent SGM a demand letter that contained assertions with which SGM disagreed. As a matter of law, such allegations do not bespeak fraud. The attorney's demand letter was protected by the litigation privilege, and SGM admits it did not detrimentally rely on the letter. Thus, contrary to SGM's assertions, it has not alleged a tortious course of conduct. At most, it alleged the parties' attorneys exchanged correspondence disagreeing over SGM's obligations under the APA, which is not tortious at all. Accordingly, the Third Count is barred by the economic loss rule and should be dismissed.

Plaintiffs respectfully request that the Court dismiss the Counterclaim.

II. THE MOTION TO DISMISS SHOULD BE GRANTED

A. SGM Cannot Recover The Deposit Because It Was Non-Refundable Under The APA's Express Terms

SGM concedes (as it must) that Section 1.2 of the APA specifies four circumstances requiring a refund of the Deposit, and that none of those circumstances occurred here. Pursuant to the express terms of the APA, the Deposit was therefore "non-refundable in all events." Despite admitting that "[a] contract may not be

interpreted in a way that renders one of its provisions meaningless," SGM nonetheless asks the Court to do just that. Opp. at 18:10-17.

Specifically, SGM asks the Court to re-write Section 1.2 to add a fifth circumstance in which it could recover the otherwise "non-refundable" Deposit: in the event of a "material default" by the Seller. But those words appear nowhere in Section 1.2, and are directly contrary to the express provision that the Deposit shall be "non-refundable in all events, except as provided in Section 6.1(b) or Section 6.2, or in the event Purchaser has terminated this Agreement pursuant to Section 9.1 (other than Section 9.1(b)) or as set forth in Section 9.2 […]."

SGM artfully asserts that Section 9.2 "states that SGM's $30 million deposit must be returned in the event of a termination under APA § 9.1[.]" Opp. at 18:18-23. In doing so, SGM omits four critical contract terms that demonstrate the fallacy of its position. Section 9.2 actually states that the Deposit must be returned if the APA "is terminated pursuant to […] 9.1 (other than Section 9.1(b))." Section 9.1 (other than Section 9.1(b)) would only apply in the event "[SGM] has terminated this Agreement." FAC, Ex. A, § 1.2. Here, of course, it is undisputed that SGM never terminated the APA. It was *Plaintiffs* who terminated the APA after SGM failed to close the transaction, and they did so *pursuant to Section 9.1(b)*. *See* FAC ¶¶ 88, 91, 93, 100, 107; SGM Answer ¶¶ 93, 107.

Tellingly, SGM does not address the fact that Section 1.2 appears in the first section of the APA, sets forth the definition of "Deposit," and expressly states the Deposit is "non-refundable in all events," except for the four instances set forth in Sections 6.1(b), 6.2, 9.1, and 9.2. FAC, Ex. A; *see In re Keller's Estate,* 134 Cal. App. 2d 232, 236 (1955) ("We are convinced that consideration should first be given to the order in which the provisions appear[.]"). Nor does SGM dispute that "[t]he starting point for the interpretation of any contract is the plain language of the agreement" and "[i]f the language of the contract is clear, the intent of the parties should be determined from the contract itself." *EduMoz, LLC v. Republic of*

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Mozambique, No. CV1302309MMMCWX, 2014 WL 12802921, at *7 (C.D. Cal. July 21, 2014).

Basic rules of contract interpretation mandate that the APA be interpreted in a manner that gives effect to each of its provisions. *E.g., Brinderson–Newberg Joint Venture v. Pac. Erectors, Inc.*, 971 F.2d 272, 278–79 (9th Cir. 1992). SGM admits this point. *See* Opp. at 18:10-17. This means that Section 11.2 must be interpreted in a way that harmonizes with Section 1.2, and there is only one way to do so. As its placement in the contract suggests, Section 11.2 merely outlines the remedies available in the event of a termination under Section 9.1(b) or (d). *See* FAC, Ex. A, § 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"). SGM's assertion that "the full text" of Section 9.2 "does not nullify" Section 11.2 misses the point, because the two provisions can be and must be interpreted in a consistent manner. Opp. at 17:12-14. SGM blatantly disregards Section 1.2 and fails to offer any competing interpretation of the APA that would give effect to the express terms of Section 1.2. *See Hints v. Am. Family Life Assurance Co. of Columbus*, No. 4:19-CV-03764-YGR, 2020 WL 2512234, at *3 (N.D. Cal. May 15, 2020) ("A court cannot rewrite the contract […]").

Nor is there any merit to SGM's assertion that Plaintiffs' interpretation means "the APA would be illusory, because Debtors would have no obligations with respect to SGM's $30 million," or would result in "an impermissible forfeiture of SGM's $30 million." Opp. at 19:3-4, 16-17. First, the Debtors' correct interpretation of the APA with respect to the Deposit does not render the APA illusory. An "illusory" contract is clearly-defined under California law: "A contract is unenforceable as illusory when one of the parties has the unfettered or arbitrary right to modify or terminate the agreement or assumes no obligations thereunder" or "where one party provides no legal consideration." *Harris v. TAP Worldwide, LLC*, 248 Cal. App. 4th 373, 385 (2016) (collecting cases). SGM does not address this strict definition and,

instead, cites to (i) general principles of contract interpretation without analysis, and (ii) inapplicable cases with distinguishable facts. *See* Opp. at 16. Far from illusory, the APA specifically delineates the limited circumstances under which the Debtors would be required to return the Deposit—and those circumstances simply did not occur. SGM cannot (and does not) allege that these provisions grant the Debtors the "unfettered or arbitrary right to modify or terminate" the APA.

Second, the Debtors retention of the Deposit is not an "impermissible forfeiture." The cases cited by SGM, again without analysis, are inapposite because each deals with the enforceability of express liquidated damages or forfeiture provisions. *See* Opp. at 16:17-21. The APA contains no such express provision, and, if it did, the provision would not be impermissible simply because it effectuated a forfeiture of the Deposit. *See In re Kitchen*, 192 Cal. 384, 389-90 (1923); *accord Urban Props. Corp. v. Benson, Inc.*, 116 F.2d 321, 323 (9th Cir.1940). Assuming, *arguendo*, that the retention of the deposit is a forfeiture, SGM does not substantively contend that the Deposit is an *impermissible* forfeiture, *i.e.*, an unenforceable penalty under California law. *See Grand Prospect Partners, L.P. v. Ross Dress for Less, Inc.*, 232 Cal. App. 4th 1332, 1358 (2015). The Debtors' retention of the Deposit under the express terms of the APA is not a penalty because the hundreds of millions of dollars of harm caused by SGM far exceeds the Deposit. *See Greentree Fin. Grp. V. Execute Sports, Inc.*, 163 Cal. App. 4th 495, 497 (2008), *as modified* (May 28, 2008).

If SGM truly believed Plaintiffs materially breached the APA, it could have terminated the APA and sought the return of its Deposit at that time. The APA did not, however, permit SGM to refuse to close the sale based on fabricated default allegations, while at the same time insisting that Plaintiffs were bound by the APA and prohibited from selling the Hospitals to other buyers. The purpose of the APA—approved and overseen by the Bankruptcy Court—was to compel a timely sale of distressed hospitals to SGM, which had agreed to buy those hospitals "AS IS, WHERE IS." SGM expressly agreed that it "is not relying on any representation or

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warranty (express or implied, oral or otherwise) made on behalf of any [Plaintiff] other than as expressly set forth in this Agreement," that the APA "shall be construed according to its fair meaning and as if prepared by all parties hereto," and that the APA is the parties' "Entire Agreement." APA §§ 3.2, 3.6, 12.9, 12.14. *See Bishay v. Icon Aircraft, Inc.*, No. 2:19-CV-00178-KJM-AC, 2020 WL 5518411, at *3 (E.D. Cal. Sept. 14, 2020.

Further, SGM's cursory discussion of the rules governing ambiguous contracts is misplaced. *See* Opp. at 19:22-21:1. An ambiguity analysis is warranted only where there are two competing interpretations of a contract, both of which give meaning and effect *to the contract as a whole*. *See Commercial Ventures, Inc. v. Scottsdale Ins. Co.*, No. CV1508359BROPJWX, 2017 WL 1196462, at *8 n.11 (C.D. Cal. Mar. 22, 2017). Here, however, SGM fails to articulate any competing interpretation of the APA that would give meaning and effect to the "non-refundable in all events" language of Section 1.2. *See Horath v. Hess*, 225 Cal. App. 4th 456, 464 (2014); *GSI Tech., Inc. v. United Memories Inc.*, No. 5:13-CV-01081-PSG, 2015 WL 5655092, at *13 (N.D. Cal. Sept. 25, 2015). Accordingly, there is no basis for an ambiguity analysis.

Finally, SGM's conclusory assertion that it may recover the Deposit as an element of contract damages is contrary to both the APA and applicable law. *See* Opp. at 21:3-9. A party cannot claim as damages amounts that are expressly non-recoverable by the terms of the contract. *See NavCom Tech., Inc. v. Oki Elec. Indus. Co.*, No. 5:12-CV-04175-EJD, 2014 WL 991102, at *11 (N.D. Cal. Mar. 11, 2014), *aff'd sub nom. NavCom Tech., Inc. v. Oki Elec. Indus. Co, Ltd.*, 756 F. App'x 682 (9th Cir. 2018); *Chinese Hosp. Ass'n v. Jacobs Eng'g Grp., Inc.*, No. 18-CV-05403-JSC, 2019 WL 6050758, at *3 (N.D. Cal. Nov. 15, 2019).[3]

[3] SGM's cited case, *Rutherford Holdings, LLC v. Plaza Del Rey*, 223 Cal. App. 4th 221, 226 (2014), is inapposite. *Holdings, LLC* involved a liquidated damages provision which provided that, in the event of a breach, the counter party would be "entitled, as [its] sole and exclusive remedy, to retain the deposit as liquidated damages[.]" This case involves no such provision.

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SGM cannot recover the Deposit under the plain and unambiguous terms of the APA. Accordingly, the Court should dismiss each of SGM's Counts to the extent they are based on this theory, or alternatively strike any allegations to this effect.

B. Plaintiffs Are Prohibited By Court Orders From Releasing The Deposit.

SGM's claim that Plaintiffs breached the APA by "wrongfully withholding/retaining" the Deposit fails for an additional reason. Counterclaim, ¶¶ 55, 58, 60, 64-65, 68. SGM does not dispute that multiple orders issued by the Bankruptcy Court (the Sale Order, Final DIP Order and supplemental cash collateral orders (the "Cash Collateral Orders"), and confirmation order ("the Confirmation Order")) precluded Plaintiffs from disbursing the Deposit. Even though SGM does not dispute that the Plaintiffs were precluded from returning the deposit, SGM never requested release of the Deposit from the Bankruptcy Court, despite having every opportunity to do so. *See* Plaintiffs' RJN, Ex. B (Sale Order at ¶ 13) and Ex. C (Final DIP Order at ¶ 4).

SGM baldly asserts that these Court Orders do not "excuse" Plaintiffs' contractual performance under the APA. *See* Opp. at 21:19-23:18. Not so. The Court should not find it "wrongful" or contrary to the APA for Plaintiffs to retain the Deposit in an escrow account when doing so was indisputedly required by Court orders. *See* Plaintiffs' RJN, Exs. B-H, O-S. Indeed, the Sale Order expressly provides that, "[u]nless otherwise provided in this Sale Order, to the extent any inconsistency exists between the provisions of the APA and this Sale Order, the provisions contained in this Sale Order shall govern." *Id.*, Ex. B (Sale Order at ¶ 26). Accordingly, the requirements of the Sale Order (including the prohibition on releasing the Deposit) control over any terms of the APA.

In addition to the Sale Order and the Cash Collateral Orders in existence prior to the filing of this action, SGM recently agreed to the language in the Confirmation Order, the joint plan of liquidation, and related disclosure statement (approved by the

Bankruptcy Court) that explicitly restricts Plaintiffs' ability to "distribute" or otherwise "take any action" regarding the Deposit without a judgment or court order. *See* Plaintiffs' RJN, Ex. N (Omnibus Reply at 6-7); *id.*, Ex. O (Disclosure Statement at 43); *id*., Ex. P (SGM Limited Objection at 1-2); *id.*, Ex. Q (Order on SGM Limited Objection at 4). Plaintiffs cannot be liable under any legal theory for failing to engage in conduct that would violate specific and controlling terms of multiple court orders, particularly when the terms of those orders were agreed to by SGM.

SGM's cited cases—which were decided 43, 77, and 115 years ago—are, once again, inapposite. *Webster v. S. Cal. First Nat. Bank*, 68 Cal. App. 3d 407, 415 (1977), involved the impossibility of performance doctrine and an injunction obtained by a third party that was not a party to the contract. No such circumstances are at issue here. *Irwindale Citrus Ass'n v. Semler*, 60 Cal. App. 2d 318, 324 (1943), likewise involved the doctrine of impossibility of performance, and nowhere states (as SGM contends) that "[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." Opp. at 20:13-14. Finally, *Union Contracting & Paving Co. v. Campbell*, 2 Cal. App. 534, 537 (1905), merely held "the issuance of an injunction at the suit of a third party was not a prevention of performance by operation of law[.]" None of these cases bear any resemblance to the circumstances in this case.

In sum, Plaintiffs were obligated to hold the Deposit, pursuant to the Sale Order and Cash Collateral Orders, and are now required to hold the Deposit as SGM requested and agreed to in the Confirmation Order. Plaintiffs have not breached (and cannot breach) the APA by acting in conformance with those orders as a matter of law. Indeed, SGM recently agreed in the Confirmation Order and related documents that the Deposit would continue to be held by the Plaintiffs in a segregated account. Accordingly, Counts I, II, and III should be dismissed to the extent they are premised on this theory. In the alternative, the Court should strike all allegations that seek to impose liability for Plaintiff's alleged failure to return the Deposit to SGM.

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C. SGM Fails to Allege Claims For Other Breaches Of Contract And The Implied Covenant Of Good Faith And Fair Dealing

Plaintiffs' Motion explains that SGM fails to allege valid claims based on conduct other than Plaintiffs' alleged "wrongful[] withholding" of the Deposit. The other "breaches" alleged in the Counterclaim are conclusory, unsupported by factual allegations, and untethered from the APA's terms. In response, SGM simply proclaims that its pleading is "sufficient" under Rule 8. Not so. The allegations in the Counterclaim fall short, as they merely assert that Plaintiffs failed "to comply with [unspecified] legal requirements," failed to obtain an unspecified approval for operation of Hospitals, failed to respond to unspecified "building and safety code violations," violated "other specifically enumerated regulatory issues as set forth in the parties' correspondence," "allow[ed]" revenue to deteriorate, fail[ed] to "reserve for its accrued obligations," and "incurr[ed] post-petition liability" (collectively, the "Other Alleged Breaches"). *See, e.g.*, Counterclaim, ¶¶ 58-59, 64, 67-68.[4]

Nor does SGM identify the APA provisions that such alleged conduct supposedly violated. Remarkably, SGM declares that it is not obligated to do so. *See* Opp. at 21:21-27. This is contrary to well-established precedent, which requires SGM to "identify the specific provision of the contract allegedly breached." *Grand Fabrics International Limited v. Melrose Textile, Inc.*, No. 18-748 DSF (AFMx), 2018 WL 6112619 (C.D. Cal. 2018). Indeed, SGM's omission is no oversight, as the actual terms of the APA do not support its position. Section 1.12 expressly provides the sale was "AS IS, WHERE IS AND WITH ALL FAULTS AND NONCOMPLIANCE WITH LAWS WITH NO WARRANTIES […]," and that "ANY AND ALL SUCH OTHER REPRESENTATIONS AND WARRANTIES

[4] *See also, e.g., Yeiser Research & Dev. LLC v. Teknor Apex Co.*, 281 F. Supp. 3d 1021, 1039 (S.D. Cal. 2017); *Marina Pac. Hotel & Suites, LLC v. Kinsale Ins. Co.*, No. 2:16-CV-03255-ODW-KS, 2016 WL 10988793, at *5 (C.D. Cal. Sept. 19, 2016); *Channel v. Wilke*, No. 218CV02414MCEACPS, 2019 WL 1491646, at *5 (E.D. Cal. Apr. 4, 2019), *report and recommendation adopted*, No. 218CV02414MCEACPS, 2019 WL 2448423 (E.D. Cal. June 12, 2019).

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ARE HEREBY EXPRESSLY DISCLAIMED […] THE ASSETS AND THE ASSUMED OBLIGATIONS ARE BEING ACQUIRED OR ASSUMED AS IS, WHERE IS ON THE CLOSING DATE AND IN THEIR PRESENT CONDITION." Unable to overcome the impact of this provision, SGM simply ignores it.

Plaintiffs' Motion explains that SGM fails to allege any damages caused by the Other Alleged Breaches because SGM does not allege that it would have closed the transaction absent such alleged conduct. Once again, SGM simply declares that it need not do so. *See* Opp. at 22:7-10. And once again, SGM's position is contrary to law: causation and damages are essential elements of SGM's claims, and must be alleged to satisfy Rule 8. *See, e.g.*, *DCR Mktg., Inc. v. U.S. All. Grp., Inc.*, No. SACV1901897JVSDFMX, 2020 WL 3883276, at *3 (C.D. Cal. June 26, 2020); *Hellenic Petroleum LLC v. Elbow River Mktg. LTD.*, No. 119CV00483LJOSKO, 2019 WL 6114892, at *4 (E.D. Cal. Nov. 18, 2019) (analyzing pleading standards under Rule 8). Thus, the remainder of SGM's claims for breach of contract and the implied covenant in Counts I, II, and III should be dismissed.[5]

D. Count III, For Tortious Breach Of Contract, Fails On Additional Grounds.

SGM cites *Underwriters at Lloyd's v. Abaxis, Inc.*, No. 19-CV-02945-PJH, 2020 WL 1677341, at *3 (N.D. Cal. Apr. 6, 2020) (quoting *Robinson Helicopter Co. v. Dana Corp.*, 34 Cal. 4th 979, 990 (2004)), for the proposition that 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 severe, unmitigable harm in the form of mental anguish, personal hardship, or substantial damages." As that same case confirms, the foundational requirement for

[5] *See Smith v. Barrett, Daffin, Frappier, Treder & Weiss, LLP*, No. 18-CV-06098-RS, 2019 WL 2525185, at *9 (N.D. Cal. June 19, 2019); *Architectural Res. Grp., Inc. v. HKS, Inc.*, No. C 12-5787 SI, 2013 WL 568921, at *3 (N.D. Cal. Feb. 13, 2013).

such a claim is "*tortious conduct* that is independent of the breach of contract claims." *Id.* at *5 (emphasis added). Absent factual allegations of tortious conduct, a tortious breach claim is barred by the economic loss rule. *Id.*

Here, the only references to allegedly "tortious conduct" in the Counterclaim (and SGM's Opposition) is SGM's assertion that Plaintiffs engaged in "fraud" and "deceit" by sending the November 20, 2019 demand letter. *See* Opp. at 23:10-11; Plaintiffs' RJN, Ex. T. But, SGM does not dispute the November 20 demand letter referenced the Bankruptcy Court's November 18 memorandum, which held that Section 8.6 of the APA had been satisfied, as the Plaintiffs had obtained an order with the requisite findings required under the APA. Thus, the statement related to Section 8.6 is not a "false" statement or a misrepresentation. Further, as SGM asserts, the demand letter referenced the settlement agreement reached the day before with the United States, on behalf of Department of Health and Human Services and the Centers for Medicare and Medicaid Services. SGM does not dispute a settlement was reached, as one was reached, consequently, this is not a "false" statement or misrepresentation. Finally, SGM admits that the Plaintiffs made no representation in the November 20 demand letter as to the California Department of Health Care Services (the "DHCS"), so there was no misrepresentation as to that issue either. No representation was necessary because Plaintiffs had already obtained orders satisfying the obligations in the APA related to DHCS. *See* FAC, ¶ 86; *see also* RJN, Ex. I at 340. Consequently, SGM's allegations that there were false statements in the November 20 demand letter must be rejected. Further, as explained in Plaintiffs' Motion, the demand letter is protected by the litigation privilege.[6]

[6] *See McNair v. City & County of San Francisco*, 5 Cal. App. 5th 1154, 1162 (2016) (citing *Silberg v. Anderson*, 50 Cal. 3d 205, 212 (1990)); s*ee I & U, Inc. v. Publishers Sols. Int'l*, 652 F. App'x 558, 559 (9th Cir. 2016); *Hedayati v. Perry Law Firm, APLC*, No. SACV1701411DOCDFMX, 2018 WL 3155186, at *5 (C.D. Cal. May 16, 2018), *report and recommendation adopted*, No. SACV171411DOCDFM, 2018 WL 3129803 (C.D. Cal. June 25, 2018); *Sandoval v. Law Office of John Bouzane*, No. 15-764, 2016 WL 7383535, *4 (C.D. Cal. Jan. 5, 2016); *Taylor v. Quall*, 458 F. Supp. 2d 1065, 1067 (C.D. Cal. 2006).

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Accordingly, contrary to SGM's assertions, it has not alleged a tortious course of conduct. Again, the only allegedly "tortious" allegations in the Third Count are the alleged "fraudulent" statements contained in counsel's November 20, 2019 demand letter which is not tortious conduct that is independent of the breach of contract claim. In contrast, Plaintiffs properly plead their tortious breach of contract claim in the First Amended Complaint. *See* FAC, ¶¶ 60, 80-87, 94-100, 115, 124-127; *see also* Order Denying Motion to Dismiss (ECF 56).

In addition, SGM fails to identify any "policy considerations [that] do not favor applying an exception to the economic loss rule." *Westport Ins. Corp. v. Vasquez, Estrada & Conway LLP*, No. 15-CV-05789-JST, 2016 WL 1394360, at *6 (N.D. Cal. Apr. 8, 2016). SGM fails to allege facts showing that Plaintiffs' alleged "conduct [was] so clearly violative of business practices, and [SGM] does not otherwise allege how the conduct breached a duty imposed by law beyond [Plaintiffs' supposed] breach of contract and breach of the covenant of good faith and fair dealing." *Id.*

Because SGM does not allege "conduct that is 'independent from the various promises made by the parties in the course of their contractual relationship,'" the Third Count is premised on "the same economic loss that it alleges in its breach of contract claim[s]." *Id.* (citing *Robinson Helicopter*, 34 Cal. 4th at 991-92). Accordingly, the economic loss rule plainly bars this claim. *See also Finney v. Ford Motor Co.*, No. 17-CV-06183-JST, 2019 WL 79033, at *5 (N.D. Cal. Jan. 2, 2019) (dismissing fraud claim under economic loss rule where no tortious breach was shown); *Finney v. Ford Motor Co.*, No. 17-CV-06183-JST, 2018 WL 2552266, at *9 (N.D. Cal. June 4, 2018) (same); *Innovative Bus. Partnerships, Inc. v. Inland Ctys. Reg'l Ctr., Inc.*, 194 Cal. App. 4th 623, 631–32 (2011).

For all of these reasons, Count III should be dismissed with prejudice.

III. CONCLUSION

For the foregoing reasons, Plaintiffs respectfully request that the Court grant their Motion to Dismiss the Amended Counterclaim.

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