UNITED STATES DISTRICT COURT

NORTHERN DISTRICT OF CALIFORNIA

ANDREW ADELMAN,

Plaintiff,

v.

U.S. SPECIALTY INSURANCE COMPANY, et al.,

Defendants.

Case No. 21-cv-02758-JST

ORDER GRANTING MOTIONS TO DISMISS

Re: ECF Nos. 24, 26

Before the Court is Defendant U.S. Specialty Insurance Company's ("U.S. Specialty") Motion to Dismiss, ECF No. 24, and Defendant Great American Insurance Company's ("Great American") Motion to Dismiss, ECF No. 26. The Court will grant the motions.

I. BACKGROUND

This case concerns the scope of insurance policies issued to Sungevity, Inc. ("Sungevity"), a now-defunct company that designed and sold residential solar panels. On March 9, 2017, Sungevity laid off approximately 330 employees and, a few days later, initiated a chapter 11 bankruptcy proceeding. On behalf of himself and a proposed class of former Sungevity employees ("Class"), Adelman filed a class action adversary proceeding against Sungevity for firing employees without notice or pay, in violation of the Worker Adjustment and Retraining Notification Act ("WARN Act") and related state employment laws. The parties settled and, as part of the settlement, the Class received an assignment of Sungevity's potential claims against certain directors and officers ("D&O").

Adelman, on behalf of the Class, and as assignee of Sungevity, then filed a suit captioned *Adelman v. Davenport, et al.*, No. RG18930626, in California state court against the D&Os for breaching their fiduciary duties of care and loyalty, and aiding and abetting breaches of these

duties ("fiduciary duty claims"). ECF No. 24-5. Defendant U.S. Specialty denied the D&Os' insurance claims and Defendant Great American reserved rights. The D&Os settled with Adelman for $4,922,510.53 and assigned their insurance claims to Adelman.

Adelman, solely in his capacity as representative of the Class, and as assignee of the D&Os, filed an action against Defendants on April 16, 2021. ECF No. 1. Adelman "seeks a declaration that Sungevity's damages were covered and a judgment in the amount of $5,297,510.53 (the settlement amount plus the Directors and Officers' attorney's fees in the State Court Action)." ECF No. 1 ¶ 16. Defendants filed the two present motions to dismiss on July 2nd, 2021. ECF Nos. 24, 26. Adelman filed an opposition, ECF No. 31, and Defendants replied, ECF Nos. 33, 34. The Court addresses both motions in this order.

II. JURISDICTION

This Court has jurisdiction pursuant to 28 U.S.C. § 1332.

III. REQUESTS FOR JUDICIAL NOTICE

Before turning to the merits, the Court addresses the parties' requests for judicial notice. "Generally, district courts may not consider material outside the pleadings when assessing the sufficiency of a complaint under Rule 12(b)(6) of the Federal Rules of Civil Procedure." *Khoja v. Orexigen Therapeutics, Inc.*, 899 F.3d 988, 998 (9th Cir. 2018). Judicial notice provides an exception to this rule. *Id.*

Pursuant to Federal Rule of Evidence 201(b), "[t]he court may judicially notice a fact that is not subject to reasonable dispute because it: (1) is generally known within the trial court's territorial jurisdiction; or (2) can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned." If a fact is not subject to reasonable dispute, the court "must take judicial notice if a party requests it and the court is supplied with the necessary information." Fed. R. Evid. 201(c)(2).

All parties in this case filed unopposed requests for judicial notice. Defendant U.S. Specialty requests judicial notice of (1) the class action complaint against Sungevity, ECF No. 24-3; (2) the settlement and release agreement between Sungevity and Adelman, ECF No. 24-4; and (3) the first amended class action complaint against the D&Os dated May 10, 2019, ECF No. 24-

5.[1] Defendant Great American requests judicial notice of (1) Defendant U.S. Specialty's Primary Insurance Policy, ECF No. 27-1; (2) Defendant Great American's Excess Insurance Policy, ECF No. 27-2; and (3) the original class action complaint against the D&Os dated November 29, 2018, ECF No. 27-3. Adelman requests judicial notice of the stipulation and order dismissing the D&O case pursuant to settlement, ECF No. 32-1. None of these documents contain disputed facts.

A court "may take judicial notice of court filings and other matters of public record." *Reyn's Pasta Bella, LLC v. Visa USA, Inc.*, 442 F.3d 741, 746 n.6 (9th Cir. 2006). Accordingly, the Court takes judicial notice of ECF Nos. 24-3, 24-4, 24-5, 27-3, and 32-1. A court may also consider "documents incorporated by reference in the complaint" at the motion to dismiss stage. *U.S. v. Richie*, 342 F.3d 903, 908 (9th Cir. 2003). Here, Adelman relies extensively on Defendants' insurance policies in the complaint. *See* ECF No. 1 ¶¶ 20-24, 87; 89-91; 93-95; 97-99; 105-110. The Court therefore takes judicial notice of Defendants' insurance policies, ECF Nos. 27-1 and 27-2.

IV. LEGAL STANDARD

A complaint must contain "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a). Dismissal under Federal Rule of Civil Procedure 12(b)(6) "is appropriate only where the complaint lacks a cognizable legal theory or sufficient facts to support a cognizable legal theory." *Mendiondo v. Centinela Hosp. Med. Ctr.*, 521 F.3d 1097, 1104 (9th Cir. 2008). A complaint need not contain detailed factual allegations, but facts pleaded by a plaintiff must be "enough to raise a right to relief above the speculative level." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007). "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face." *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quotation marks and citation omitted). "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." *Id.*

[1] Defendant U.S. Specialty also included the underlying insurance policy, ECF No. 24-2, but failed to mention the policy in its request to the Court. Regardless, the Court takes judicial notice of the policy pursuant to Defendant Great American's request. ECF No. 27.

In determining whether a plaintiff has met this standard, the court must "accept all factual allegations in the complaint as true and construe the pleadings in the light most favorable" to the plaintiff. *Knievel v. ESPN*, 393 F.3d 1068, 1072 (9th Cir. 2005).

V. DISCUSSION

The underlying facts in this case are not in dispute. At issue is the scope of two exclusionary clauses in the insurance policy: Exclusion (F), an insured-versus-insured exclusion, and/or Exclusion (L), an exclusion of certain employment law claims.

A. California Rules of Interpretation

California law governs the interpretation of the insurance policy at issue in this case because California is the forum state of this diversity action. *See Encompass Ins. Co. v. Coast Nat'l Ins. Co.*, 764 F.3d 981, 984 (9th Cir. 2014) ("California's substantive insurance law governs in this diversity case.") (internal quotation marks and citation omitted); *Bell Lavalin, Inc. v. Simcoe & Erie Gen. Ins. Co.*, 61 F.3d 742, 745 (9th Cir. 1995) (applying forum state's law to policy interpretation in diversity action).

In California, "[i]nterpretation of an insurance policy is a question of law and follows the general rules of contract interpretation." *Waller v. Truck Ins. Exch., Inc.*, 900 P.2d 619, 627 (Cal. 1995). California courts "must give effect to the 'mutual intention' of the parties . . . at the time the contract is formed." *Id.* This intent should be inferred, whenever possible, from the four corners of the contract and terms should be interpreted in the "ordinary and popular sense." *MacKinnon v. Truck Ins. Exch.*, 31 Cal. 4th 635, 647-48 (2003). A provision that can reasonably be interpreted in more than one way must be interpreted in favor of the insured. *Clarendon Am. Ins. Co. v. N. Am. Capacity Ins. Co.*, 186 Cal. App. 4th 556, 567 (2010). Additionally, California courts interpret coverage broadly and exclusions narrowly, in order to give the greatest possible protection to the insured. *Jeff Tracy, Inc. v. U.S. Specialty Ins. Co.*, 636 F. Supp. 2d 995, 1002 (C.D. Cal. 2009).

B. Exclusion (L)

The key issue here is whether the fiduciary duty claims are barred by Exclusion (L). Exclusion (L) provides:

> [T]he Insurer will not be liable to make any payment of **Loss** in connection with a **Claim**:
>
> (L) for any actual or alleged violation of any provision of the Fair Labor Standards Act other than the Equal Pay Act, the National Labor Relations Act, the Worker Adjustment and Retraining Notification Act, the Consolidated Omnibus Budget Reconciliation Act of 1985, the Occupational Safety and Health Act, any workers' compensation, unemployment insurance, social security or disability benefits law or any amendments thereto, or any other similar provisions of any federal, state or local statutory or common law or any rules and regulations promulgated under any of the foregoing; provided, that this EXCLUSION (L) shall not apply to any **Claim** for any actual or alleged **Retaliation**.

ECF No. 27-1 at 60 (emphasis in original). Defendants argue that the fiduciary duty claims are barred by Exclusion (L) because the fiduciary duty claims were brought "in connection with" violations of the WARN Act. ECF No. 24 at 13; *see also* ECF No. 26 at 14-17. Adelman claims that Exclusion (L) does not apply to the fiduciary duty claims because the "[t]he Employment Claims and the Fiduciary Duty Claims are not the same 'Claim,'" ECF No. 31 at 22, and because "[a]n exclusion does not bar all factually related fiduciary duty claims," ECF No. 31 at 26. The dispute centers on the meaning of the phrase "in connection with."

"In connection with" is synonymous with the phrase "arising out of." *Ambrosio v. Certain Underwriters at Lloyd's Under Pol'y No. B0146ldusa0701030*, No. C 11-04956 RS, 2012 WL 12540015, at *7 (N.D. Cal. Mar. 29, 2012). And "arising out of" is "ordinarily understood to mean 'originating from,' 'having its origins in,' 'growing out of,' or 'flowing from' or in short, 'incident to, or having connection with.'" *Davis v. Farmers Ins. Grp.*, 134 Cal. App. 4th 100, 107 (2005) (cleaned up); *see also Cont'l Cas. Co. v. City of Richmond*, 763 F.2d 1076, 1080-81 (9th Cir. 1985) (same). California courts have found that the plain language of "in connection with" creates something lower than a strict "but-for" requirement. *See Zurich Specialties London Ltd. v. Bickerstaff, Whatley, Ryan & Burkhalter, Inc.*, 650 F. Supp. 2d 1064, 1070 (C.D. Cal. 2009) (finding that the plain language of "arising out of" could not reasonably be interpreted to create a "but-for" requirement).

Under California law, the phrase "in connection with" "does not import any particular . . . theory of liability into an insurance policy." *Acceptance Ins. Co. v. Syufy Enters.*, 69 Cal. App.

4th 321, 328 (1999). A court examining an insurance policy exclusion that uses the term "in connection with" must "examine the conduct underlying the . . . lawsuit, instead of the legal theories attached to the conduct." *Century Transit Sys., Inc. v. American Empire Surplus Lines Ins. Co.*, 42 Cal. App. 4th 121, 127 n.4 (1996) (internal quotations and citation omitted). Thus, that the two claims are not the "same claim" and "are based on independent and unrelated bodies of law" with "different elements," as Adelman contends, has no bearing on this analysis. *See* ECF No. 31 at 22-23. Instead, the phrase "in connection with" "broadly links a factual situation with the event creating liability and connotes only a minimal causal connection or incidental relationship." *Acceptance*, 69 Cal. App. 4th at 328.

Although the Court has not located any California Supreme Court or appellate court case analyzing whether fiduciary duties are "connected with" the WARN Act, *Medill* is instructive. *See Medill v. Westport Ins. Corp.*, 143 Cal. App. 4th 819 (2006). In *Medill*, a case cited by both parties, the court found that insurance carriers properly rejected coverage of fiduciary duty claims against directors and officers. *Id.* at 822. The *Medill* plaintiffs argued that a contract exclusion provision did not apply because they asserted negligence and breach of fiduciary duty claims, not a breach of contract claim. *Id.* at 829. The court rejected their argument, instead finding that the negligence and breach of fiduciary duty claims arose out of the contract because "the directors' and officers' potential liability would not exist without the contracts." *Id.* at 830.

As in *Medill*, the claims in this case also meet the higher "but-for" standard because the D&Os' potential liability would not exist without an alleged violation of the WARN Act. To reach this conclusion, the Court need only look to Adelman's complaint in *Adelman v. Davenport*, where he alleged the following:

> "Those claims involve questions of common or general interest, in that they assert that Defendants breached their fiduciary duties to Sungevity by causing the company to undergo the mass layoff of March 9, 2017, without complying with the WARN Act, the California WARN Act, and the California and Missouri wage-payment laws." ECF No. 24-5 ¶ 91.

- "Defendants were well aware of Sungevity's statutory obligations regarding the WARN Act and related state laws due to Defendants' collective, regular, and repeated receipt of legal advice from outside and inside counsel." *Id.* ¶ 95.

- Defendants "thus breached their duty of loyalty by causing or allowing a mass layoff of the Class on March 9, 2017, without complying with the WARN Act and California WARN Act notice requirements or California and Missouri wage-payment laws." *Id.* ¶ 97.

- Defendants' "actions and decisions disregarded Sungevity's statutory obligation to provide WARN Act notices, giving rise to a WARN Act claim against Sungevity." *Id.* ¶ 98.

- Defendants "breached their fiduciary duties to Sungevity when they caused or allowed a mass layoff of the Class on March 9, 2017, without complying with the WARN Act and California WARN Act notice requirements or California and Missouri wage-payment laws." *Id.* ¶ 103.

- Defendants' "actions and decisions disregarded Sungevity's statutory obligation to provide WARN Act notices, giving rise to a WARN Act claim against Sungevity." *Id.* ¶ 104.

- Defendants "knew or should have known of Sungevity's statutory obligations regarding the WARN Act and related state laws." *Id.* ¶ 105.

- "Defendants breached their fiduciary duties to Sungevity when they caused or allowed the company to conduct a mass layoff of the Class on March 9, 2017, without complying with the WARN Act and California WARN Act notice requirements or California and Missouri wage-payment laws." *Id.* ¶ 111.

Adelman argues that the mere mention of a subject is not enough to trigger an exclusion. That contention is correct, so far as it goes. But Adelman did more than mention the WARN Act. Each of Adelman's claims rested on the assumption that the D&Os either knowingly or negligently violated the WARN Act when they conducted a mass layoff.[2] Because Adelman's fiduciary duty claims only exist due to alleged violations of the WARN Act, the Court finds that the fiduciary duty claims were made "in connection with" alleged violations of the WARN Act and are covered by Exclusion (L).[3]

[2] The Court is not persuaded by Adelman's citations to out-of-circuit cases where courts determined that a contract exclusion did not bar coverage for fiduciary duty claims. ECF No. 31 at 26. These cases are not binding and are contradicted by other out-of-circuit cases where courts found that coverage for fiduciary duty claims was barred by contract exclusions. ECF No. 34 at 14. Nor is the Court persuaded by *Hanover Ins. Co. v. Paul M. Zagaris, Inc.*, 714 F. App'x 735 (9th Cir. 2018) (mem.). Beyond the limitations inherent in relying on a memorandum disposition, *Grimm v. City of Portland*, 971 F.3d 1060, 1067 (9th Cir. 2020), the case is also distinguishable on its facts. In *Hanover*, the allegations in the case created a potential for liability on grounds unrelated to the excluded conduct. The same is not true here.

[3] That Adelman's complaint includes claims for "California and Missouri wage-payment laws" does not change the Court's conclusion. Exclusion (L) unambiguously states that it applies to the WARN Act and "any other similar state provisions." Adelman concedes that these state laws are "related" to the WARN Act. ECF No. 24-5 ¶¶ 6-7, 9, 28, 30, 43, 95, 99, 105-07.

Courts have found that the purpose of exclusionary language in similar provisions "is to avoid 'moral hazard,' which, in its most extreme form, is the temptation of the insured to precipitate the event insured against." *See California Diaries Inc. v. RSUI Indem. Co.*, 617 F. Supp. 2d 1023, 1035 (E.D. Cal. 2009) (internal quotations and citation omitted). For example, in *Farmers Auto. Ins. Assoc. v. St. Paul Mercury Ins. Co.*, 482 F.3d 976, 978 (7th Cir. 2007), Judge Posner explained that the Fair Labor Standards Act exclusion prevented the employer from unjustly enriching itself by "refus[ing] to pay overtime and then invok[ing] coverage so that the cost of the overtime would come to rest on the insurance company." The same public policy rationale applies here. If the Court held that the WARN Act Exclusion in this case did not encompass closely related fiduciary duty claims, D&Os could fire employees without notice or pay, knowing that the insurance company would protect them. "No insurance company would knowingly write a policy that would enable the insured to trigger coverage any time it wanted a windfall." *Id*. at 979. Therefore, both public policy and the plain language of the statute lead to the same conclusion: Adelman's fiduciary duty claims are barred by Exclusion (L).[4]

CONCLUSION

Although it appears unlikely that Adelman would be able to cure the identified deficiencies by amendment, the Court grants leave to amend out of an abundance of caution. Adelman may file an amended complaint within 21 days, solely to correct the deficiencies identified in this order. If no amended complaint is filed by that date, the complaint will be dismissed with prejudice.

The case management conference scheduled for November 23, 2021 is continued to

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[4] Because Exclusion (L) bars the fiduciary claims, the Court does not reach the question of whether the fiduciary duty claims are also covered by Exclusion (F).

January 25, 2022 at 2:00 p.m. An updated joint case management statement is due January 18, 2022.

IT IS SO ORDERED.

Dated: November 17, 2021

JON S. TIGAR
United States District Judge