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United States District Court, N.D. California,
San Francisco Division.

Mark TARAKANOV and Nelya Tarakanov, Plaintiffs,
v.
LEXINGTON INSURANCE COMPANY, Defendant.

Case No. 19-cv-05666-LB
|
Signed 02/26/2020

Synopsis
Background: Insureds who lost their home during wildfire brought action against home insurer alleging insurer failed to accept claim for extended replacement-cost coverage and alleging claims for breach of contract, breach of the implied covenant of good faith and fair dealing, fraudulent concealment based on insurer's alleged concealment of difficulty of claims for extended replacement-cost reimbursement, and a violation of California's Unfair Competition Law (UCL) predicated on the alleged fraud. Insurer filed motion to dismiss.

Holdings: The District Court, Laurel Beeler, United States Magistrate Judge, held that:

insureds failed to allege insurer breached obligations by denying hypothetical claim for extended replacement-cost coverage;

insureds failed to allege insurer breached the covenant of good faith and fair dealing by failing to accept claim, delaying response, and refusing to acknowledge coverage obligations; and

insureds failed to allege insurer fraudulently concealed material facts regarding its extended replacement-cost coverage.

Motion granted.

Attorneys and Law Firms

John Francis Frost, Paul Timothy Llewellyn, Lewis Llewellyn LLP, San Francisco, CA, for Plaintiffs.

James P. Wagoner, Lejf E. Knutson, Nicholas H. Rasmussen, McComick Barstow Sheppard Wayte & Carruth LLP, Fresno, CA, for Defendant.

ORDER GRANTING MOTION TO DISMISS

Re: ECF No. 18

LAUREL BEELER, United States Magistrate Judge

INTRODUCTION

***1** This is an insurance-coverage dispute. The plaintiffs lost their home in Napa during the 2017 Northern California wildfires. [1] They bought an insurance policy from defendant Lexington Insurance that included replacement-cost coverage (for the value of the lost or damaged dwelling) and extended replacement-cost coverage ("ERC coverage") (for the cost to repair or replace the lost or damaged dwelling). [2] Lexington paid the plaintiffs the replacement value of their home but denied their ERC claim because they did not repair or replace their home. The plaintiffs then sued Lexington, claiming breach of contract, breach of the implied covenant of good faith and fair dealing, fraudulent concealment (based on Lexington's alleged concealment of the difficulty of claims for ERC reimbursement), and a violation of California's Unfair Competition Law ("UCL") predicated on the alleged fraud. [3]

Lexington moved to dismiss the claims under Federal Rule of Civil Procedure 12(b)(6), in part on the ground that a condition precedent to its obligation to pay ERC — and a fact allegation missing from the complaint — was the plaintiffs' repair or replacement of their home. [4] The plaintiffs responded that their claim of breach is not Lexington's failure to disburse funds and instead is Lexington's failure to accept their claim for ERC coverage. [5] Because the insurance contract does not impose that obligation, the court grants Lexington's motion to dismiss the contract-based claims. The court dismisses the fraud claims because the plaintiffs did not plausibly plead concealment of a material fact regarding ERC claims.

STATEMENT

1. The Insurance Policy

On October 3, 2017, the plaintiffs bought a home with three acres of land in Napa, California.[6] The next day, they purchased homeowner's insurance from Lexington.[7] The policy provided coverage for damage to the property caused by fire and contained the following coverages: (1) replacement-cost coverage; (2) ERC coverage; and (3) Building Code Upgrade Coverage ("Ordinance coverage").[8] The coverage limits were $1,500,000.00 for "Dwelling;" $150,000.00 for "Other Structures;" $300,000.00 for "Contents;" and $150,000.00 for "Loss of Use."[9] The policy contained the following notice regarding "Demand Surge:"

> After a widespread disaster, the cost of construction can increase dramatically as a result of the unusually high demand for contractors, building supplies and construction labor. This *effect* is known as demand surge. Demand surge can increase the cost of rebuilding your home. Consider increasing your coverage limits or purchasing Extended Replacement Cost coverage to prepare for this possibility.[10]

***2** The policy's ERC coverage provided up to $750,000 in coverage in the event of loss or damage to the home and provided that the plaintiffs "elect[ed] to repair or replace the damaged building."[11] ERC coverage was subject to the following:

> Subparagraph 2. of Paragraph **C. Loss Settlement (SECTION I - CONDITIONS)** is deleted in its entirety and replaced with the following:
>
> 2. Buildings covered under Coverage **A** at replacement cost without deduction for depreciation, subject to the following:
>
> ...
>
> d. We will pay no more than the actual cash value of the damage until actual repair or replacement is complete. Once actual repair or replacement is complete, we will settle the loss as noted in **2.a**. and **b**. above.[12]

The Ordinance Coverage provision provided the following:

> **11. Ordinance Or Law**
>
> **a.** You may use up to 10% of the limit of liability that applies to Coverage **A** for the increased costs you incur due to the enforcement of any ordinance or law which requires or regulates:
>
> **(1)** The construction, demolition, remodeling, renovation or repair of that part of a covered building or other structure damaged by a Peril Insured Against;
>
> ...
>
> **c.** We do not cover:
>
> **(1)** The loss in value to any covered building or other structure due to the requirements of any ordinance or law; or
>
> ...
>
> This coverage is additional insurance.[13]

2. The Wildfires and Coverage Claims

On October 8, 2017, a massive wildfire spread across Napa, Butte, Lake, Mendocino, and Solano Counties and completely destroyed the plaintiffs' home, among thousands of others.[14]

On October 11, 2017, the plaintiffs submitted a property-loss notice to Lexington.[15] Lexington assigned an independent adjusting firm, which inspected the property and determined that it was a total loss.[16] It paid the plaintiffs $2,121,597.05 for the loss of their home and damage to their surrounding property.[17] Lexington did not pay ERC or Ordinance coverage.[18]

The plaintiffs allegedly "elected to rebuild their destroyed home" and "incurred costs and made other expenditures associated with the initial rebuilding efforts."[19] They faced obstacles to their rebuilding efforts.[20] In addition to the plaintiffs, thousands of people in Napa, Solano, and Sonoma

Counties, and others throughout Northern California, were rebuilding.[21] As a result, there was an overwhelming demand for architects, contractors, and construction workers, who often were victims of the fire too, which bogged down the permitting process.[22] The situation was particularly acute in Napa.[23] In a survey of Napa County residents, 17% reported that they would not rebuild, and 67% (of the 17%) reported that "their insurance company was restricting their benefits to buy elsewhere, in part because insurance companies were not willing to pay ERC Coverage or Ordinance Coverage."[24] "In other words, at the time of the ... report, the Tarakanovs were among hundreds of homeowners for whom it was impossible to make meaningful progress on rebuilding their Home due to the effects of Demand Surge. Yet — like so many other homeowners in the region, the Tarakanovs had not received the additional ERC Coverage and Ordinance Coverage that Lexington Insurance had recommended to address these effects, and that was necessary for the Tarakanovs to rebuild."[25]

***3** The next section is titled "The Tarakanovs are Forced to Sell Their Home," and in it, the plaintiffs allege the following:

> 41. On December 21, 2018, the Tarakanovs sent a letter to Lexington Insurance again requesting coverage under the ERC Coverage and Ordinance Coverage provisions.
>
> 42. Several months passed without a response from Lexington Insurance. In the intervening time, the Tarakanovs were left in limbo with no indication by Lexington that it would cover the Tarakanovs' costs under the ERC Coverage or Ordinance Coverage should they proceed with the rebuilding. This uncertainty was particularly acute given the Demand Surge and resulting Loss Amplification, as the Tarakanovs could not be sure that Lexington would not attempt to deny their claims due to the increased construction costs then prevailing in Northern California.
>
> 43. The Tarakanovs understood Lexington's failure to respond to their inquiry as an indication that it was rejecting their claim for reimbursement of repair and replacement costs. As a result of Lexington's failure to accept their claim under ERC Coverage and Ordinance Coverage provisions, in the face of mounting future rebuilding expenses, and without any assurance that Lexington would fully honor the Tarakanovs' policy and cover replacement costs, the Tarakanovs had no choice but to sell the Property for $1,075,000 less than the price for which they had purchased it.[26]

They then allege that "[o]n March 11, 2019 — nearly three full months after the Tarakanovs had inquired regarding acceptance of their replacement and ordinance coverage claims — Lexington Insurance finally responded to the Tarakanovs' December 21, 2018 letter. In that response, Lexington Insurance confirmed that it was rejecting the Tarakanovs' ERC Coverage and Ordinance Coverage claim."[27]

Lexington submits the parties' actual correspondence, which the court considers under the incorporation-by-reference doctrine. *Knievel v. ESPN*, 393 F.3d 1068, 1076–77 (9th Cir. 2005). The correspondence shows the parties' communications during the window — between December 21, 2018 and March 11, 2019 — when the plaintiffs sold their property.

By a letter emailed to AIG Claims (Lexington's claim administrator)[28] on December 21, 2018, the plaintiffs' then-counsel requested ERC and Ordinance coverage and demanded payment of $750,000 for ERC coverage and $150,000 for Ordinance coverage.[29]

AIG acknowledged receipt by email that day.[30] On January 9, 2019, the plaintiffs' counsel asked for an update about the timing of AIG's response, and AIG — cc'ing coverage counsel, who is defense counsel of record in this lawsuit — responded that it had retained coverage counsel, who would be responding shortly.[31] On February 7, 2019, Lexington's counsel wrote to the plaintiffs' counsel:

> ***4** As you know from prior email correspondence from Lexington Insurance Company ("Lexington"), this office and the undersigned have been retained by Lexington to assist it in its analysis, evaluation and resolution of this claim. I acknowledge both your correspondence dated December 21, 2018 and your email to Lexington dated January 9, 2019,.
>
> We are completing our review, analysis and evaluation of the facts and circumstances surrounding this claim, the applicable policy provisions and the relevant legal authorities. I expect to have a letter prepared to address the matters raised by your correspondence dated December 21, 2018, shortly.[32]

On March 11, 2019, Lexington sent a letter to the plaintiffs declining "to extend payment *at this time*" under the ERC coverage and Ordinance coverage provisions:

> Based on a review of all relevant facts, circumstances, the Policy and the law, Lexington respectfully declines to extend payment *at this time* for additional coverage under the Extended Replacement Cost Coverage ("ERC Coverage"). In addition, Lexington reserves all other potential coverage defenses as well as the potential application of any and all policy terms, conditions, limitations or exclusions. Lexington will consider a supplemental claim for indemnification under the ERC Coverage once the requisite conditions for such coverage have been met, subject to all other terms, conditions, limitations and exclusions of the Policy.[33]

In the letter, coverage counsel summarized the relevant facts and policy provisions and explained Lexington's coverage position.[34] He acknowledged the plaintiffs' position that, while they took "early and immediate costly steps to carry out th[eir] intent" to replace their home, "Demand Surge" factors made it "factually and *legally* impractical and/or impossible at the present time."[35] He also acknowledged the plaintiffs' position that it was unreasonable for Lexington to require the plaintiffs to begin construction before any ERC coverage payment was made, and he disagreed with that position.[36] Citing legal authority, he said that "Lexington's current coverage position [is] that its duty to pay the additional amount of insurance under the ERC Endorsement has not yet arisen" because under the policy's terms, actual replacement and repair are conditions precedent to disbursement of ERC amounts under the ERC Endorsement.[37] Thus, Lexington "is only obligated to pay the actual cash value of the damage," capped at $1,500,000.[38] He concluded that the plaintiffs' difficulties in the building and permitting process were temporary difficulties, and not a real impossibility, and thus did not excuse the plaintiffs' obligation to begin the repairs and replacement in order to obtain ERC funds.[39] He also explained Lexington's rejection of the Ordinance Coverage.[40] He concluded:

> In conclusion, Lexington respectfully declines payment, *at this time*, under ERC Coverage in the ERC Endorsement until the condition precedent for the application of such coverage has been satisfied. Additionally, Lexington respectfully declines payment, *at this time*, under the Ordinance or Law Coverage provision of the Policy until there is credible evidence of the costs the insured have incurred or will be obligated to incur due to the enforcement of any actual "ordinance or law," as defined in *Bischel* [*v. Fire Ins. Exchange*, 1 Cal. App. 4th 1168, 1175, 2 Cal.Rptr.2d 575 (1991)].[41]

***5** The letter concluded with the following.

> Please be advised that, in addition to declining payment at this time as explained above, Lexington reserves the right to limit or disclaim coverage or payment on any other ground which may become known. Lexington expressly reserves all rights, remedies and defenses available under the policy, at law, in equity and/or under public policy, including, without limitation, the right to raise additional policy provisions and other available defenses or limitations to coverage should that become necessary. Nothing contained herein, nor any other activity on the part of Lexington in connection with the investigation or handling of this matter, shall constitute a waiver, relinquishment or forfeiture of any rights with respect to coverage and the policy, and all rights are expressly reserved. The insureds should not interpret any actions taken by Lexington as an admission or concession that the policy provides particular coverage for this claim.
>
> Any investigation conducted by Lexington is subject to all the terms, conditions, provisions and limitations of the

policy. Nothing herein shall be construed as a waiver any of the policy's terms, provisions, conditions or limitations.

Please note that Lexington is reserving all rights based on the information presently in its possession. In the event that the insureds possess any information which they believe may influence the determinations of coverage, we invite its prompt, written submission. However, any further investigation or evaluation of coverage by Lexington is made subject to a complete reservation of rights, including the right to alter or amend this coverage position upon the receipt of further material information and does not constitute a waiver or modification of the coverage position stated herein unless they are expressly notified otherwise, in writing.

The Policy includes a condition which limits the insureds' time to file suit concerning the claim:

G. Suit Against Us

No action can be brought against us unless there has been full compliance with all of the terms under Section **I** of this policy and the action is started within one year after the date of loss.

There may also be other statutes of limitation which are applicable to this claim. To the extent any limitation period may have been tolled or suspended before the date of this letter, such tolling or suspension is deemed to end effective with the date of this letter.

If the insureds believe this claim has been wrongfully declined or rejected, in whole or in part, or that there is a dispute as to liability or damages, they have the right for the matter to be reviewed by the California Department of Insurance. Direct all correspondence to: California Department of Insurance, Claims Services Bureau, 11th Floor, 300 Spring Street, Los Angeles, CA 90013, (213) 897-8921 or (800) 927-4357. [42]

3. Lexington's Alleged Scheme to Avoid Paying Replacement Costs

The complaint has the following fact allegations under a section titled "Lexington's Scheme to Avoid Covering Replacement Costs:"

***6** 49. On information and belief, Lexington Insurance's position — that it may reject claims under the ERC Coverage and Ordinance Coverage provisions pending completion of replacement and repairs — comprises a deliberate scheme to avoid paying these kinds of insurance coverage under its insurance policies in the face of widespread destruction due to natural disaster.

50. As discussed above, the Consumer Notice Disclosure accompanied the Policy. Due to the inclusion of the Consumer Notice Disclosure, Lexington Insurance must know that its policies inform its Lexington customers that widespread disasters can create a Demand Surge, which inflate the costs and difficulty of rebuilding in the wake of a disaster. On information and belief, Lexington Insurance is also aware that a Demand Surge can create excessive delays in rebuilding after total loss due to widespread natural disaster.

51. On information and belief, by refusing to honor the Tarakanovs' ERC Coverage and Ordinance Coverage in the immediate wake of a mass disaster, Lexington sought to simultaneously (1) discourage the Tarakanovs from rebuilding, as they would be forced to do so without assurance that Lexington would ultimately honor their claim for replacement coverage, and (2) terminate any equitable tolling of the one-year time limit after the loss for the Tarakanovs to bring a claim against Lexington. Meanwhile the circumstances of a Demand Surge after a mass disaster can make it virtually impossible to complete rebuilding within a one-year timeframe—as noted above, a one year progress report issued by Napa County showed that only a single home had been rebuilt out of 653 destroyed, while in nearby Sonoma County only 40 of over 5000 homes had been rebuilt. Since completion of rebuilding would only have occurred more than a year after Lexington's initial denial, Lexington would be free to ignore its obligations under the ERC Coverage and Ordinance Coverage provisions, and the Tarakanovs would lack any legal recourse to enforce the provisions.

52. On information and belief, Lexington has developed a scheme that allows the company to insulate itself from repair and replacement costs in the face of widespread disaster, despite its contractual obligations. First, Lexington denies claims for repair and replacement costs in the immediate wake of the loss, arguing that this action starts the clock on the one-year contractual limitation on actions against the company. Lexington does this in the knowledge that the Demand Surge will likely make rebuilding within the one-year timeframe effectively impossible. If the insured does choose to rebuild and submits a claim after completion, Lexington can deny

coverage and rely on the one-year limitation to dismiss any action against the company for breaching its obligations under the insurance agreement.

53. Put simply, if Lexington's interpretation of its contractual obligations holds true, it has devised a strategy to make its ERC Coverage and Ordinance Coverage provisions illusory should the insured's property be lost as part of a widespread disaster event like that suffered by the Tarakanovs. On information and belief, hundreds—if not thousands—of homeowners throughout the state who have lost homes to wildfires have been defrauded by this same scheme, by Lexington and by other insurance carriers. [43]

4. Procedural History

***7** The plaintiffs filed this lawsuit on September 9, 2019. [44] The parties consented to magistrate-judge jurisdiction. [45] In their operative complaint, the plaintiffs claim the following: (1) breach of contract (based on Lexington's actions denying ERC and Ordinance coverage); (2) breach of the covenant of good faith and fair dealing (also based on Lexington's denial of the claims, refusal to acknowledge its obligation to cover repair and replacement costs, and forcing the plaintiffs to contemplate rebuilding their home without an assurance that Lexington would honor their repair claims); (3) fraudulent concealment (for, among other reasons, Lexington's knowledge that it is too difficult to make an ERC claim and concealing that knowledge from the plaintiffs); and (4) unfair competition, in violation of the UCL, Cal. Bus. & Prof. Code § 17200, *et seq.* (by its scheme to ignore its obligation to honor ECR and Ordinance coverage, thereby starting the contractual one-year limitations for any lawsuits regarding its denial of claims). [46]

Lexington moved to dismiss the claims under Federal Rule of Civil Procedure 12(b)(6). [47] The court held a hearing on February 13, 2020. [48]

STANDARD OF REVIEW

A complaint must contain a "short and plain statement of the claim showing that the pleader is entitled to relief" to give the defendant "fair notice" of what the claims are and the grounds upon which they rest. Fed. R. Civ. P. 8(a)(2); *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007). A complaint does not need detailed factual allegations, but "a plaintiff's obligation to provide the 'grounds' of his 'entitlement to relief' requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do. Factual allegations must be enough to raise a claim for relief above the speculative level ...." *Twombly*, 550 U.S. at 555, 127 S.Ct. 1955 (internal citations omitted).

To survive a motion to dismiss, a complaint must contain sufficient factual allegations, which when accepted as true, " 'state a claim to relief that is plausible on its face.' " *Ashcroft v. Iqbal*, 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009) (quoting *Twombly*, 550 U.S. at 570, 127 S.Ct. 1955). "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.* "The plausibility standard is not akin to a 'probability requirement,' but it asks for more than a sheer possibility that a defendant has acted unlawfully." *Id* (quoting *Twombly*, 550 U.S. at 557, 127 S.Ct. 1955). "Where a complaint pleads facts that are merely consistent with a defendant's liability, it stops short of the line between possibility and plausibility of 'entitlement to relief.' " *Id* (quoting *Twombly*, 550 U.S. at 557, 127 S.Ct. 1955) (internal quotations omitted).

"In alleging fraud ..., a party must state with particularity the circumstances constituting fraud.... Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally." Fed. R. Civ. P. 9(b). This means that "[a]verments of fraud must be accompanied by the 'who, what, when, where, and how' of the misconduct charged." *Vess v. Ciba–Geigy Corp. USA*, 317 F.3d 1097, 1106 (9th Cir. 2003). Like the basic "notice pleading" demands of Rule 8, a driving concern of Rule 9(b) is that defendants be given fair notice of the charges against them. *In re Lui*, 646 F. App'x 571, 573 (9th Cir. 2016) ("Rule 9(b) demands that allegations of fraud be specific enough to give defendants notice of the particular misconduct ... so that they can defend against the charge and not just deny that they have done anything wrong.") (quotation omitted); *Odom v. Microsoft Corp.*, 486 F.3d 541, 553 (9th Cir. 2007) (Rule 9(b) requires particularity "so that the defendant can prepare an adequate answer").

If a court dismisses a complaint, it should give leave to amend unless the "pleading could not possibly be cured by the allegation of other facts." *Yagman v. Garcetti*, 852 F.3d 859, 863 (9th Cir. 2017) (citations and internal quotation marks omitted).

ANALYSIS

1. Breach of Contract

***8** Lexington moved to dismiss the breach-of-contract claim on the grounds that (1) the plaintiffs did not allege that they repaired or rebuilt their home (and actually did not), which is a condition precedent to Lexington's obligation to pay ERC and Ordinance coverage; and (2) the plaintiffs' claim for anticipatory breach — which is predicated on Lexington's failure to confirm that it would pay ERC and Ordinance coverage if the plaintiffs rebuilt — fails because Lexington never refused performance.[49] The plaintiffs countered that they do not claim that Lexington breached the policy by failing to disburse replacement costs and instead claim that it breached the policy

> by failing to accept their claim for replacement coverage when tendered under the Policy. In sum, Defendant's breach is for the failure to accept Plaintiffs' claim for repair and replacement costs when presented, and acknowledge its obligation to reimburse Plaintiffs for repair costs once incurred. As alleged in the FAC, this breach forced the Plaintiffs to sell their property at a loss, incurring damages.[50]

The court grants Lexington's motion because the plaintiffs do not plausibly plead that Lexington breached its obligations under the insurance policy.

In California, courts apply contract law to interpret insurance policies:

> Interpretation of an insurance policy is a question of law and follows the general rules of contract interpretation. (*Waller v. Truck Ins. Exchange, Inc.* (1995) 11 Cal. 4th 1, 18, 44 Cal. Rptr. 2d 370, 900 P.3d 619 (*Waller*).) The fundamental rules of contract interpretation are based on the premise that the interpretation of a contract must give effect to the mutual intention of the parties. Under statutory rules of contract interpretation, the mutual intention of the parties at the time the contract is formed governs interpretation. (Civ. Code, § 1636). Such intent is to be inferred, if possible, solely from the written provisions of the contract. (*Id.*, § 1639). The clear and explicit meaning of these provisions, interpreted in their ordinary and popular sense, unless used by the parties in a technical sense or a special meaning is given to them by usage (*id.*, § 1644), controls judicial interpretation. (*Id.*, § 1638.) [Citations.] A policy provision will be considered ambiguous when it is capable of two or more constructions, both of which are reasonable. [Citation.] But language in a contract must be interpreted as a whole, and in the circumstances of the case, and cannot be found to be ambiguous in the abstract. (*Id.* at p. 18, 44 Cal. Rptr. 2d 370, 900 P.2d 619.)
>
> Moreover, insurance coverage is interpreted broadly so as to afford the greatest possible protection to the insured, [whereas] ... exclusionary clauses are interpreted narrowly against the insurer. (*White v. Western Title Ins. Co.* (1985) 40 Cal. 3d 870, 881, 221 Cal. Rptr. 509, 710 P.2d 309.) ... The burden is on the insured to establish that the claim is within the basic scope of coverage and on the insurer to establish that the claim is specifically excluded. (*Aydin Corp. v. First State Ins. Co.* (1998) 18 Cal. 4th 1183, 1188, 77 Cal. Rptr. 2d 537, 959 P.2d 1213.)

MacKinnon v. Truck Ins. Exchange, 31 Cal. 4th 635, 647–48, 3 Cal.Rptr.3d 228, 73 P.3d 1205 (2003) (internal quotations omitted).

"A court may resolve contractual claims on a motion to dismiss if the terms of the contract are unambiguous." *Ellsworth v. U.S. Bank, N.A.*, 908 F. Supp. 2d 1063, 1084 (N.D. Cal. 2012) (citing *Barrous v. BP P.L.C.*, No. 10-CV-2944-LHK, 2010 WL 4024774 (N.D. Cal. Oct. 13, 2010); *Bedrosian v. Tenet Healthcare Corp.*, 208 F.3d 220 (9th Cir. 2000)). "By contrast, what the parties intended by an ambiguous contract is a factual determination, *United States v. Plummer*, 941 F.2d 799, 803 (9th Cir. 1991), and thus '[w]here the language leaves doubt as to the parties' intent, the motion to dismiss must be denied.' " *Id.* (quoting *Monaco v. Bear Stearns Residential Mortg. Corp.*, 554 F. Supp. 2d 1034, 1040 (C.D. Cal. 2008)); *see also Trustees of Screen Actors Guild–Producers Pension and Health Plans v. NYCA, Inc.*, 572 F.3d 771, 777 (9th Cir. 2009).

***9** The plaintiffs do not dispute that Lexington did not breach the policy when it failed to disburse replacement

costs.[51] Their claim is that Lexington had an obligation to acknowledge its obligation to reimburse, or put differently, accept the plaintiffs' hypothetical claim.[52] This theory does not plausibly establish a breach of contract.

First, in the December 21, 2018 letter, the plaintiffs' then-counsel did not ask Lexington to acknowledge its obligation or accept a hypothetical claim. He asked for disbursement of the ERC and Ordinance funds.[53] Lexington denied the claim, which was premature because the plaintiffs had not repaired or rebuilt their home.

Second, the timeline of the parties' correspondence — summarized in the Statement — does not support the plaintiffs' allegations that Lexington failed to respond to the December 21 demand, thereby breaching the contract and forcing the plaintiffs to sell their home. The plaintiffs allege that they (1) asked about coverage on December 21, 2018, (2) were "left in limbo" with no indication that Lexington would cover their costs, (3) "understood Lexington's failure to respond to their inquiry as an indication that it was rejecting their claim," and (4) "[a]s a result of Lexington's failure to accept their claim..., in the face of mounting rebuilding expenses, and without any assurance that Lexington would fully honor the ... policy and cover replacement costs," they "had no choice but to sell the property...." But Lexington acknowledged the December 21 letter the same day and provided coverage counsel's contact information on January 9, 2019 (in response to the plaintiffs' counsel's earlier email that day).[54] Coverage counsel sent a letter on February 7, 2019, saying that he was completing his review and expected to have a response to the December 21 letter shortly.[55] On March 11, 2019, he wrote a detailed letter explaining his coverage position.[56] This short timeline is not "limbo," a failure to respond, or a situation that forced the plaintiffs to sell their home in the window between December 21, 2018 and March 11, 2019.

Third, as coverage counsel explained in his March 11, 2019 letter, Lexington's duty to pay the ERC coverage had "not yet arisen" because under the policy's terms, actual repair and replacement are conditions precedent to disbursement of ERC funds, and Lexington denied the claim for payment "at this time" until the plaintiffs satisfied the conditions precedent.[57] Lexington similarly denied the claim for Ordinance coverage "at this time."[58] Lexington's counsel explained the grounds for his decision, and the plaintiffs (again) do not dispute that payment was premature.

Instead, to support their argument that Lexington had a duty to accept their claim, the plaintiffs cite *Milhouse v. Travelers Com. Ins. Co.* 982 F. Supp. 2d 1088 (C.D. Cal. 2013). There, the court held that "the triggering of obligations under a replacement coverage provision may occur separately and prior to the time for actual disbursement of replacement costs."[59] *Id.* at 1096–97. But the policy in *Milhouse* provided coverage when the Millhouses "elect[ed]" to rebuild their insured property. *Id.* at 1096. The policy here is different: it required the insureds to repair, rebuild, or replace the property as a condition precedent to payment. Moreover, the Millhouses' entitlement to the replacement coverage at issue was predicated on an "actual cash value" of their loss that exceeded the policy limit. *Id.* at 1096–97. The court held that because replacement coverage was available as soon as the insureds "elected" to rebuild, Travelers had to pay them the face value of the policy and the additional amounts (under the replacement-coverage provision) up to the full actual cash value" (or the policy limits). *Id.* The court limited this entitlement to the "actual cash value": "Of course, until the home is rebuilt, under the policy, the Millhouses are entitled to no more than the actual cash value of the home." *Id.* at 1097.

***10** The plaintiffs also argue that coverage counsel's inclusion of the "Suit Against Us" clause in his letter (excerpted in the Statement) changes the outcome — and requires Lexington's assurance that it will accept a future claim — because it establishes that the denial ended any tolling period and started the clock on the one-year contractual limitations period.[60] Lexington does not dispute that it denied the claim that the plaintiffs made (immediate payment of ERC and Ordinance coverage) and that the denial triggered the one-year contractual limitations period for bringing a lawsuit.[61] But that reality does not create any duty by Lexington to assure the plaintiffs that it would fulfill its obligations under the policy. Again, the policy defines Lexington's obligations to pay claims, the plaintiffs do not dispute that they did not satisfy the condition precedent (rebuilding or replacing their home) to Lexington's obligation to pay ERC and Ordinance coverage, and Lexington explained that its denial did not preclude a claim once the plaintiffs satisfied the condition precedent. Nothing in the record suggests that Lexington is playing "gotcha."

At the hearing, part of the discussion centered on California's regulatory scheme that defines an insurer's obligations to an insured. Generally, those obligations are defined in the policy. *Gibson v. Gov't Emps. Ins. Co.*, 162 Cal. App. 3d 441, 449–50, 208 Cal.Rptr. 511 (1984) ("any fiduciary duty between an insurer and insured is governed by the terms of the insurance contract in effect between them"). The duty that the plaintiffs posit here — an insurer's duty to prospectively accept a claim predicated on the insured's future performance of a condition precedent — is not a disclosure obligation under the policy or California's regulatory scheme. No case supports the plaintiffs' position. Given the regulatory scheme that governs here, creating a duty to prospectively accept a claim is not appropriate.

Moreover, the facts (in the complaint and the parties' correspondence) do not establish that Lexington anticipatorily breached its duties by forcing a situation where the plaintiffs could not satisfy the condition precedent within the one-year limitations period. The plaintiffs sold their property in the short time between December 21, 2018 to March 11, 2019, before the denial of payment. [62] The facts that they plead do not establish impossibility.

The plaintiffs also contend that the policy allows them to make a claim for replacement within 180 days of the loss, "well before the replacement for total loss could be feasibly completed...."

> e. You may disregard the replacement cost loss settlement provisions and make claim under this policy for loss to buildings on an actual cash value basis. You may then make claim for any additional liability according to the provisions of this Condition **C**. Loss Settlement, provided you notify us of your intent to do so within 180 days after the date of loss. [63]

As the defendants point out, the issue here is the claim for replacement cost, which is covered by the policy's loss-settlement provisions, and in any event, this provision requires the plaintiffs to give notice of their intent to claim replacement costs and not to actually make a premature claim. [64]

In sum, the plaintiffs do not plausibly state a claim for breach of contract.

2. Breach of the Covenant of Good Faith and Fair Dealing

***11** Because it dismisses the claim for breach of contract, the court dismisses this claim too.

Generally, "without a breach of the insurance contract, there can be no breach of the implied covenant of good faith and fair dealing." *Manzarek v. St. Paul Fire & Marine Ins. Co.*, 519 F.3d 1025, 1034 (9th Cir. 2008) (citing *Waller v. Truck Ins. Exch.*, 11 Cal. 4th 1, 36, 44 Cal.Rptr.2d 370, 900 P.2d 619 (1995)); *see also Love v. Fire Ins. Exch.*, 221 Cal. App. 3d 1136, 1153, 271 Cal.Rptr. 246 (1990).

The claim for breach of the covenant is predicated on Lexington's alleged wrongful failure to accept the plaintiffs' claim, its delayed response to the plaintiffs' correspondence, and its refusal to acknowledge its coverage obligations. [65] As the court held in the previous section, there is no duty to accept a hypothetical claim, Lexington in any event described its coverage position and willingness to accept a supplemental claim, and it responded promptly to the plaintiffs' counsel's inquiries. The plaintiffs thus do not plausibly state a claim for breach of the covenant of good faith and fair dealing.

3. Fraudulent Concealment

The elements of fraudulent concealment are "(1) concealment or suppression of a material fact; (2) by a defendant with a duty to disclose the fact to the plaintiff; (3) the defendant intended to defraud the plaintiff by intentionally concealing or suppressing the fact; (4) the plaintiff was unaware of the fact and would not have acted as he or she did if he or she had known of the concealed or suppressed fact; and (5) the plaintiff sustained damage as a result of the concealment or suppression of the fact." *Dent v. Nat'l Football League*, 902 F.3d 1109, 1125 (9th Cir. 2018) (quoting *Hambrick v. Healthcare Partners Med. Grp., Inc.*, 238 Cal. App. 4th 124, 189, 189 Cal.Rptr.3d 31 (2015)).

The alleged fraud here is that Lexington knew that it was too difficult for homeowners to make claims for ERC reimbursement after a natural disaster, intentionally

concealed that information from the plaintiffs, had the obligation to disclose its knowledge, and intended to defraud the plaintiffs through the scheme to avoid paying ERC coverage. [66]

The plaintiffs do not plausibly state a claim. First, the policy does warn of "Demand Surge" after a widespread disaster, resulting in increased costs of construction and high demand for contractors, building supplies, and construction labor. [67] Second, the allegations are conclusory. Third, the facts do not suggest fraudulent concealment. The timeline — from the demand letter on December 21, 2018 to the coverage opinion on March 11, 2019 — was short. The coverage letter explained the coverage position thoroughly and denied the claim "at this time." The Napa fires were a natural disaster. The allegations do not suggest an attempt to duck ERC coverage, much less fraudulently conceal a material fact.

4. UCL Claim

The plaintiffs predicate the UCL claim on Lexington's fraudulent concealment. [68] They contend that they suffered injury-in-fact when they sold their property at a loss "as a result of Defendant's improper conduct, and when they paid for coverage that was not functionally available." [69] Because the plaintiffs do not plausibly plead a claim for fraudulent concealment, they do not plead plausibly plead a UCL claim.

CONCLUSION

***12** The court grants Lexington's motion to dismiss. The plaintiffs may file an amended complaint within 21 days of the date of this order. If they file an amended complaint, they must also file as an attachment a blackline of their new amended complaint against their current FAC. If they do not file an amended complaint, the dismissal will be with prejudice, and the court will enter judgment in favor of Lexington. This disposes of ECF No. 18.

The court asks the parties to confer and submit an update within seven days from the date of this order about their views about a further court-sponsored ADR process, including a mediation with the court's ADR program or a referral for a settlement conference with a magistrate judge. If the parties say that they want a settlement conference, they should say why, and they may specify a specific judge or ask for a random referral.

IT IS SO ORDERED.

All Citations

--- F.Supp.3d ----, 2020 WL 1059211

Footnotes

1 First Am. Compl. ("FAC") – ECF No. 13 at 4 (¶ 19–21); Policy, Ex. A to FAC – ECF No. 13 at 68. Citations refer to material in the Electronic Case File ("ECF"); pinpoint citations are to the ECF-generated page numbers at the top of documents.
2 FAC – ECF No. 13 at 2–3 (¶¶ 8–17); Policy, Ex. A to FAC – ECF No. 13 at 68.
3 FAC – ECF No. 13.
4 Mot. – ECF No. 17 at 8–10.
5 Opp'n – ECF No. 20 at 7.
6 FAC – ECF No. 13 at 2 (¶ 7).
7 *Id.* (¶ 8) (the policy took effect on October 5, 2017); Policy, Ex. A to FAC – ECF No. 13 at 16–114.
8 *Id.* at 2 (¶ 10), at 3 (¶ 13); Policy, Ex. A to FAC – ECF No. 13 at 68 (capitalization in original).
9 Policy, Ex. A to FAC – ECF No. 13 at 19.
10 FAC – ECF No. 13 at 3 (¶ 16) (quoting Policy, Ex. A to FAC – ECF No. 13 at 69) (emphasis in original).
11 *Id.* at 3 (¶ 17). Policy, Ex. A to FAC – ECF No. 13 at 80. ERC coverage provides an additional amount of coverage equal to 50% of the Coverage A limit, which was $1,500,000. *Id.* at 19.
12 Policy, Ex. A to FAC – ECF No. 13 at 80–81.
13 *Id.* at 37.
14 FAC – ECF No. 13 at 4 (¶¶ 20–21).
15 *Id.* (¶ 24).
16 *Id.* (¶ 25).

17 *Id.* (¶ 26); Sullivan Letter, Ex. A to Hansen Decl. – ECF No. 17-1 at 9. The court considers the Sullivan Letter under the incorporation-by-reference doctrine. *Knievel v. ESPN*, 393 F.3d 1068, 1076–77 (9th Cir. 2005).
18 FAC – ECF No. 13 at 4 (¶ 26).
19 *Id.* at 5 (¶ 27).
20 *Id.* (¶ 28).
21 *Id.*
22 *Id.* (¶¶ 29–30).
23 *Id.* (¶ 33).
24 *Id.* at 6 (¶ 39).
25 *Id.* (¶ 40).
26 *Id.* at 6–7 (¶¶ 41–43).
27 *Id.* at 7 (¶ 44).
28 Hansen Decl. – ECF No. 17–1 at 2 (¶ 3).
29 Sullivan Letter, Ex. 1 to Hansen Decl. – ECF No. 17-1 at 4–8 (four outstanding claims; the primary two were ERC coverage ($750,000) and Ordinance coverage ($150,000); the two other claims were Coverage C (Contents) and Coverage D (Loss of Use) (but the letter acknowledged that AIG had not denied its obligation to make payments under these Coverages)); Email, Ex. 3 to Suppl. Hansen Decl. – ECF No. 21-1 at 8.
30 Email, Ex. 3 to Suppl. Hansen Decl. – ECF No. 21-1 at 7.
31 *Id.* at 5–6.
32 Hansen Letter, Ex. 4 to Suppl. Hansen Decl. – ECF No. 21-1 at 10.
33 Hansen Letter, Ex. 2 to Hansen Decl. – ECF No. 17-1 at 11 (emphasis in original).
34 *Id.* at 12–30.
35 *Id.* at 22 (quoting and citing the December 21, 2018 demand letter).
36 *Id.*
37 *Id.* at 22–23.
38 *Id.*at 24–25 (capitalization omitted).
39 *Id.* at 26–27.
40 *Id.* at 28–29 (the plaintiffs did not identify the code or regulation triggering increased costs or offer credible evidence of cost).
41 *Id.* at 29.
42 *Id.* at 29–30.
43 FAC – ECF No. 13 at 9–10 (¶¶ 49–53).
44 Compl. – ECF No. 1.
45 Consents – ECF Nos. 6, 10.
46 FAC – ECF No. 13 at 10–13 (¶¶ 54–78).
47 Mot. – ECF No. 18.
48 Minute Entry – ECF No. 31.
49 Mot. – ECF No. 18 at 19–24.
50 Opp'n – ECF No. 20 at 7–8.
51 Opp'n – ECF No. 20 at 12–14.
52 *Id.*
53 Letter – Ex. 1 to Hansen Decl. – ECF No. 17-1 at 4–8 (summarized in Statement).
54 Emails, Ex. 3 to Suppl. Hansen Decl. – ECF No. 21-1 at 5.
55 Hansen Letter, Ex. 3 to Suppl. Hansen Decl. – ECF No. 21-1 at 10–11.
56 Hansen Letter – Ex. 2 to Hansen Decl. – ECF No. 17-1.
57 *Id.* at 22–23, 29 (summarized in Statement).
58 *Id.* at 28–29.
59 Opp'n – ECF No. 20 at 13–14.
60 Opp'n – ECF No. 20 at 17–18.

61 Hansen Letter – Ex. 2 to Hansen Decl. – ECF No. 17-1 at 11, 29; *see* Reply – ECF No. 21 at 15 (does not dispute this point and observes that by law, it had to include the provision in its letter denying the claim) (quoting Cal. Code Reg. § 2695.4(a) ("Every insurer shall disclose to a first party claimant or beneficiary, all benefits, coverage, time limits or other provision of any insurance policy issued by that insurer that may apply to the claim presented by the claimant.")).

62 As discussed at the hearing, there is an established way that ERC coverage is paid (generally, in installments after work begins and interim inspections are held).

63 Opp'n – ECF No. 20 at 15; *see* Policy, Ex. A to FAC – ECF No. 13 at 81.

64 Reply – ECF No. 21 at 13.

65 Opp'n – ECF No. 20 at 20.

66 FAC – ECF No. 13 at 9–10 (¶¶ 49–53), 11–12 (¶¶ 63–74).

67 Policy, Ex. A to FAC – ECF No. 13 at 69.

68 FAC – ECF No. 13 at 13 (¶¶ 75–78); Opp'n – ECF No. 20 at 26–27.

69 Opp'n – ECF No. 20 at 26.