Watts v. Allstate Indemnity Company et al Doc. 79

UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

ROBERT WATTS, on behalf
of himself individually and
all others similarly situated,

Plaintiff,

v.

ALLSTATE INDEMNITY CO.,
an Illinois corporation, et al.,

Defendants.
_______________________________/

NO. CIV. S-08-1877 LKK/GGH

O R D E R

Defendants in this action are Allstate Indemnity Company, Allstate Insurance Company, and Allstate Property and Casualty Insurance Company. Plaintiff Robert Watts allegedly had an automobile insurance policy with one or more defendants. His car was involved in an accident, after which he sought replacement of the seatbelts and associated mechanisms. Defendants allegedly refused to pay for these costs or to engage in related actions. Plaintiff then filed this putative class action alleging six claims. By a prior order, this court granted defendants' motion

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to dismiss plaintiff's claim under Racketeer Influenced and Corrupt Organizations Act ("RICO") and denied defendant's motion as to all other claims. Plaintiff's RICO claim was dismissed without prejudice, and plaintiff has filed a Second Amended Complaint re-pleading this claim. Defendants then filed a motion to dismiss this amended claim. For the reasons stated below, this motion is granted, and plaintiff's RICO claim is again dismissed without prejudice.

I. BACKGROUND

A. Factual Background[1]

Plaintiff's factual allegations in his Second Amended Complaint ("SAC") are substantially similar to those in his First Amended Complaint ("FAC"), except for the allegations specific to plaintiff's RICO claim. These allegations are discussed in greater detail in this court's order of March 31, 2009, Doc. No. 66, 2009 U.S. Dist. LEXIS 26618. An abbreviated version of these allegations is provided here.

The SAC, like the FAC, names three defendants: Allstate Indemnity Company, Allstate Insurance Company, and Allstate Property and Casualty Insurance Company. Also like the FAC, the SAC uses the name "Allstate" to refer to all three defendants collectively, and thereby brings most allegations against all three defendants, and does not specify which role was played by which

[1] The following facts are taken from the allegations of plaintiff's second amended complaint, and are treated as true for purposes of this motion only.

defendant.

Pursuant to this practice, plaintiff alleges that he purchased and/or renewed an auto policy from "Allstate" in late 2005. SAC ¶ 39. At that time and now, Allstate's standardized materials assured policyholders that "accidents happen," but that policyholders would "continue to feel the safety Allstate provided from the beginning." Id. ¶ 29. Allstate's slogan was and is "You're in good hands with Allstate." Part VII of the auto policy received by plaintiff provides that "Allstate will pay for direct and accidental loss to your insured auto . . from a collision with another object or by upset of that auto . . . ." Defs.' Ex. A, Policy, 18.

On March 29, 2006, plaintiff's insured vehicle was involved in a collision. SAC ¶ 42. This impact damaged the seatbelts and associated mechanisms. Id. ¶¶ 16, 42. Defendants nonetheless refused to provide insurance coverage to replace the seatbelts. ¶ 53.

Allstate's refusal to pay for seatbelt replacement was the result of "a uniform policy of refusing to pay for seat belt replacement and inspection in any Allstate-insured vehicle involved in an automobile accident." Id. ¶ 22. Allstate acted to conceal this policy. Id. "Allstate . . . trained its employees to avoid writing the inspection or repair of seat belts into estimates for repair of vehicles involved in a collision." Id. ¶ 23. This policy was adopted pursuant to a recommendation by a consulting group, McKinsey, which led to:

> universal, company-wide policies and procedures in place at ALLSTATE to arrive at powerful, cost-saving tools to systematically deny, reduce, or minimize the amount of money paid on personal injury and property damage claims including the corporate-wide policy to deny the inspection and replacement of seat belts in postcollision ALLSTATE-insured vehicles.

Id. ¶ 38.

B. Procedural History

Plaintiff's RICO claim is alleged under 18 U.S.C. § 1962(c).[2] This section provides that:

> It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

18 U.S.C. § 1962(c). In granting defendants' motion to dismiss plaintiff's RICO claim as alleged in the FAC, this court explained that plaintiff had alleged that "Allstate" was both the "person" and the "enterprise" for purposes of section 1962(c), but that the statute required two separate entities. Order of April 20, 2009 at 24-25. In the SAC, plaintiff alleges that defendant Allstate Indemnity Company is the "person," and that defendant Allstate Insurance Company is the "enterprise." SAC ¶¶ 114, 115. The former is a subsidiary of the latter. Id. at ¶ 116. Plaintiff

[2] Although the SAC merely refers to section 1962, plaintiff's opposition memorandum clarifies that plaintiff's claim arises only under section 1962(c).

attributes the policy of declining to inspect and replace seatbelts to Allstate Indemnity Company (the alleged “person”), alleging that this policy constitutes fraud, and increases profits for both Allstate Indemnity Co. and Allstate Insurance Co. Id. ¶¶ 117, 118. This fraudulent policy was created and implemented in Illinois, and “is passed along state lines through every ALLSTATE office in the United States and every ALLSTATE- owned auto repair shop.” Id. ¶¶ 119, 120. Plaintiff’s RICO claim further alleges that “Allstate” engages in fraud every time it informs prospective policyholders that it will return their vehicle to safe, pre-accident conditions. Id. ¶ 121. Lastly, plaintiff alleges that “ALLSTATE uses its considerable leverage to prevent third party autorepair shops across the country from inspecting or repairing the seat belts in ALLSTATE-insured post-collision vehicles.” Id. ¶ 122.

II. STANDARD FOR A FED. R. CIV. P. 12(B)(6) MOTION TO DISMISS

In order to survive a motion to dismiss for failure to state a claim, plaintiffs must allege "enough facts to state a claim to relief that is plausible on its face." Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 569 (2007). While a complaint need not plead "detailed factual allegations," the factual allegations it does include "must be enough to raise a right to relief above the speculative level." Id. at 555.

The Supreme Court recently held that Federal Rule of Civil Procedure 8(a)(2) requires a "showing" that the plaintiff is entitled to relief, “rather than a blanket assertion” of entitlement to relief. Id. at 555 n.3. Though such assertions may

provide a defendant with the requisite "fair notice" of the nature of a plaintiff's claim, the Court opined that only factual allegations can clarify the "grounds" on which that claim rests. Id. "The pleading must contain something more. . . than . . . a statement of facts that merely creates a suspicion [of] a legally cognizable right of action." Id. at 555, quoting 5 C. Wright & A. Miller, Federal Practice and Procedure, § 1216, pp. 235-36 (3d ed. 2004).[3]

On a motion to dismiss, the allegations of the complaint must be accepted as true. See Cruz v. Beto, 405 U.S. 319, 322 (1972). The court is bound to give the plaintiff the benefit of every reasonable inference to be drawn from the "well-pleaded" allegations of the complaint. See Retail Clerks Int'l Ass'n v. Schermerhorn, 373 U.S. 746, 753 n.6 (1963). In general, the Complaint is construed favorably to the pleader. See Scheuer v. Rhodes, 416 U.S. 232, 236 (1974), overruled on other grounds by Harlow v. Fitzgerald, 457 U.S. 800 (1982). Nevertheless, the court does not accept as true unreasonable inferences or conclusory legal allegations cast in the form of factual allegations. W. Mining Council v. Watt, 643 F.2d 618, 624 (9th Cir. 1981).

III. ANALYSIS

Defendants provide five arguments for dismissal. The first

[3] The holding in Twombly explicitly abrogates the well established holding in Conley v. Gibson that, "a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." 355 U.S. 41, 45-46 (1957); Twombly, 550 U.S. at 560.

of these arguments, failure to allege racketeering activity, warrants dismissal. However, this defect may be cured by amendment. The court therefore addresses the remaining arguments as well. Doing so is necessary for evaluation of defendants' argument that these remaining grounds support dismissal with prejudice, and also avoids the need for these arguments to be raised in future motions.

A. Racketeering Activity, and A Pattern of Racketeering

First, defendants argue that plaintiff has not alleged "racketeering activity," which the statute defines with a list of enumerated offenses. 18 U.S.C. § 1961(1), H.J. Inc. v. Northwestern Bell Telephone Co., 492 U.S. 292, 232 (1989). Defendants relatedly argue that because there is no racketeering activity, there is not an allegation of a "pattern" of racketeering activity either.

Common law fraud is not racketeering activity. See Giuliano v. Fulton, 399 F.3d 381, 388 (1st Cir. 2005). However, mail fraud and wire fraud are racketeering activity. 18 U.S.C. § 1961(1)(B) (enumerating 18 U.S.C. §§ 1341 (mail fraud) and 1343 (wire fraud)). In opposing this motion, plaintiff argues that the SAC effectively alleges mail and wire fraud, by alleging that defendant's policy was both fraudulent and implemented across state lines. In the Ninth Circuit, the Fed. R. Civ. P. 9(b) pleading requirements apply to the pleading of mail and wire fraud in RICO actions. Lancaster Community Hosp. v. Antelope Valley Hosp. Dist., 940 F.2d 397, 405 (9th Cir. 1991). This requires a plaintiff to identify the

specific communications allegedly constituting mail and wire fraud. Id. (citing Moore v. Kayport Package Express, Inc., 885 F.2d 531, 541 (9th Cir. 1989)). The SAC does not identify any such communications, and therefore fails to allege racketeering activity. By extension, the SAC also fails to allege a pattern of racketeering activity. Id. (a "pattern" for RICO purposes requires at least two acts of racketeering activity).

B. No RICO Claim Is Alleged Against Allstate Insurance Co. and Allstate Property and Casualty Co.

RICO liability attaches to a "person . . . associated with any enterprise." 18 U.S.C. § 1962(c). Plaintiff's complaint explicitly alleges that the "person" in plaintiff's section 1962(c) claim is "Allstate Indemnity Company." Plaintiff alleges that Allstate Insurance Company played the role of the enterprise--a role to which RICO liability does not attach--and plaintiff makes no allegations concerning the role played by Allstate Property and Casualty Insurance Company. Accordingly, plaintiff fails to state a RICO claim against these two defendants. However, it also appears that plaintiff may cure this defect through amendment. For example, plaintiff may be able to properly allege that each defendant was a person conducting the affairs of an association in fact enterprise, composed of certain of the companies.

The court expresses no opinion as to whether possible future allegations of this particular type are consistent with plaintiff's understanding of the facts and whether they would support such a claim; in particular, plaintiff would need to address how the

alleged person conducted the affairs of the alleged enterprise, as discussed below. The court merely cannot yet conclude that all possible allegations various defendants as RICO "persons" would be futile.

C. Distinctiveness between the "Person" and "Enterprise"

Defendants also argue that a parent corporation is not distinct from its subsidiary for purposes of a section 1962(c) claim. Section 1962(c) requires a person "associated with" an enterprise. 18 U.S.C. § 1962(c). Courts have held that because an entity cannot associate with itself, this language imposes a "distinctness" requirement, such that the person must be distinct from the enterprise. See Cedric Kushner Promotions, Ltd. v. King, 533 U.S. 158, 160 (2001), Wilcox v. First Interstate Bank, N.A., 815 F.2d 522, 529 (9th Cir. 1987). In other words, the "'enterprise' [can] not simply [be] the same 'person' referred to by a different name." King, 533 U.S. at 160. See also River City Markets, Inc. v. Fleming Foods West, Inc., 960 F.2d 1458, 1461 (9th Cir. 1992) ("The person / enterprise distinction arises from the long-standing common law maxim that a person cannot conspire with himself.").

Unpopular statutes often develop unusual jurisprudence. Thus, in decisions of several other circuits, corporate subsidiaries were found not to be distinct from their corporate parents. See Bucklew v. Hawkins, Ash, Baptie & Co., LLP, 329 F.3d 923, 934 (7th Cir. 2003), Bessette v. Avco Financial Services, Inc., 230 F.3d 439, 449 (1st Cir. 2000), Fogie v. THORN Americas, Inc., 190 F.3d 889, 898

(8th Cir. 1999), Brannon v. Boatmen's First Nat'l Bank, 153 F.3d 1144, 1147 (10th Cir. 1998) Lorenz v. CSX Corp., 1 F.3d 1406, 1412 (3d Cir. 1993). As recently explained by Judge Sabraw in the Southern District of California:

> These courts recognize that the parent and its subsidiary are separate legal entities. However, they also acknowledge that "a subsidiary that simply conducts its affairs as delegated by the parent company for the profit of the parent company is engaged in nothing more than a legitimate corporate and financial relationship, which is certainly not subject to RICO liability on that basis alone." Bessette, 230 F.3d at 449 (citations omitted). Accordingly, these courts require "something more" to satisfy the distinctiveness requirement.

Leyvas v. Bank of Am. Corp. (In re Countrywide Fin. Corp. Mortg. Mktg. & Sales Practices Litig.), 601 F. Supp. 2d 1201, 1214 (S.D. Cal. 2009) (citing cases from the First, Third, Seventh, and Eighth Circuits).

Neither the Ninth Circuit nor the Supreme Court have directly addressed this issue. C.f. Wilcox v. First Interstate Bank, N.A., 815 F.2d 522, 529-30 (9th Cir. 1987) (declining to rule on whether a parent corporation could be the enterprise in a section 1962(c) claim against a subsidiary). However, both have considered closely related cases. In United States v. Benny, 786 F.2d 1410 (9th Cir. 1986), the Ninth Circuit held that the owner of a sole proprietorship was distinct from the proprietorship for purposes of 18 U.S.C. section 1962(c). Id. at 1415. The court stated in dicta that the sole stockholder of a corporation was distinct from the corporation, because the corporation's separate existence

provides "some legal protections," and because all that is required for distinctness "'is that the [enterprise] be either formally (as when there is corporation) or practically (as when there are other people beside the proprietor working in the organization) separable from the individual.'" Id. at 1416 (quoting McCullough v. Suter, 757 F.2d 142, 144 (7th Cir. 1985), modification in original); accord Emery v. American Gen. Fin., 134 F.3d 1321, 1325 (7th Cir. 1998) ("there is no contradiction or even strain in talking about the 'owner' of a 'corporation' as separate entities."). The Ninth Circuit quoted from Benny and repeated this dicta in Sever v. Alaska Pulp Corp., 978 F.2d 1529, 1534 (9th Cir. 1992). In Sever, the Ninth Circuit again stated in dicta that a sole stockholder was separate from a corporation, and held that officers of a corporation were also distinct from the corporation itself, notwithstanding "the inability of a corporation to operate except through its officers." Id.

The Supreme Court reached a similar result in King, holding that section 1962(c) applies "when a corporate employee unlawfully conducts the affairs of the corporation of which he is the sole owner -- whether he conducts those affairs within the scope, or beyond the scope, of corporate authority." King, 533 U.S. at 166. "The corporate owner/employee, a natural person, is distinct from the corporation itself, a legally different entity with different rights and responsibilities due to its different legal status. And we can find nothing in the statute that requires more 'separateness' than that. Cf. McCullough v. Suter, 757 F.2d 142,

144 ([7th Cir.] 1985) (finding either formal or practical separateness sufficient to be distinct under § 1962(c)).” Id. at 163.[4]

In Illinois v. Countrywide Fin Corp, plaintiffs argued to the Southern District of California that the Supreme Court’s decision in King and the Ninth Circuit’s decision in Sever supported the conclusion that a parent is per se distinct from its subsidiary. 60 F. Supp. 2d at 1214 n.3. The district court rejected this argument on the ground that King and Sever did not directly consider this question. Id. Instead, the court “[found] it more appropriate to consider the reasoning of those courts that have addressed this particular issue.” Id. The court therefore held that to satisfy the distinctiveness requirement, plaintiffs most allege “something more” than the fact that a parent and subsidiary are legally separate entities. Id. at 1214. The court then held that this requirement was satisfied, because plaintiffs had alleged that the decision to act through a subsidiary removed a potential for checks and balances that would have inhibited the racketeering scheme, and that each individual had a distinctive role. Id. at 1214-15.

Plaintiff in this case has not attempted to allege “something

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[4] Thus, both the Supreme Court, in King, and the Ninth Circuit, in Sever, have favorably cited the Seventh Circuit’s decision in McCullough, which found that either formal or practical separateness sufficed. McCollough therefore carries some weight with this court notwithstanding the fact that the Seventh Circuit did not follow McCullough in concluding that a corporate parent is not ordinarily distinct from a corporate subsidiary. See, e.g., Bucklew, 329 F.3d at 934.

more" demonstrating distinctness. Nonetheless, this court must disagree with Countrywide Fin. Corp. and conclude that King and Sever control this case, and that "something more" is not required. King held that the only distinctiveness required was "a legally different entity with different rights and responsibilities due to its different legal status." 533 U.S. at 163. Sever adopted a similar test, and held that formal distinctiveness was itself sufficient, regardless of whether there was also practical separation. 978 F.2d at 1534 (quoting Benny, 786 F.2d at 1416). A separately-incorporated subsidiary satisfies the tests articulated by both King and Sever.

Two additional factors support this conclusion. Both King and Sever concluded that a sole shareholder was distinct from a corporation. King, 533 U.S. at 166; Sever, 978 F.2d at 1534. A corporate parent's relationship with a subsidiary is that of a majority, if not sole, shareholder. Therefore, King and Sever come closer to addressing these facts than Countrywide Fin. Corp. acknowledged.

Furthermore, although this court does not disregard the weight of authority from other circuits lightly, the court takes some reassurance from the Ninth Circuit's recent en banc opinion in Odom v. Microsoft Corp., 486 F.3d 541 (9th Cir. 2007). Odom reiterated that courts "should not read the statutory terms of RICO narrowly." Id. at 547. While "[t]here has been some judicial resistance to RICO, manifested in narrow readings of its provisions by lower federal courts[,] [i]n four notable cases [one of which was King],

the Supreme Court has corrected these narrow readings." Id. at 545. From these cases, the Ninth Circuit took the observation that "RICO is to be read broadly" and "be liberally construed to effectuate its remedial purposes." Id. at 547 (quoting Sedima, S.P.R.L. v. Imrex Co., 473 U.S. 479, 497-98 (1985)).

For these reasons, the court holds that a corporate parent is distinct from its corporate subsidiary such that one may be "associated with" the other for purposes of a claim under 18 U.S.C. section 1962(c).

D. The Person's Conduct of the Enterprise's Affairs

Lastly, to state a claim under section 1962(c), a plaintiff must allege that the "defendant[] conducted or participated in the conduct of the 'enterprise's affairs,' not just [its] own affairs." Reves v. Ernst & Young, 507 U.S. 170, 185 (1993). A defendant must participate in the "operation" or "management" of the enterprise, such that the defendant has "some part in directing the [enterprise's] affairs." Id. at 179, 185.

Here, plaintiff's complaint includes no allegations speaking to this issue. Plaintiff's sole argument is that "whether a particular defendant actually operates or manages an enterprise" is ordinarily a jury question. Pl.'s Opp'n, 7. While the question of whether certain conduct constitutes operation or management of an enterprise may be a jury question, such conduct must first be identified. C.f. United States v. Allen, 155 F.3d 35, 42-43 (2d Cir. 1998) ("A reasonable fact-finder could find that payment of the bribes either did or did not" constitute "participation in the

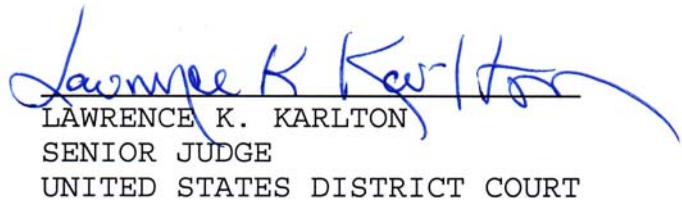
operation or management of the enterprise.”). Accordingly, to state a RICO claim under section 1962(c), plaintiff must allege that the person “conduct[ed] or participate[d]” in the enterprise’s affairs, § 1962(c), and this allegation must be more than “a formulaic recitation of the elements of a cause of action.” Twombly, 550 U.S. at 555.

IV. CONCLUSION

For the reasons stated above, defendants’ motion to dismiss is GRANTED. Plaintiff’s sixth claim for relief is hereby DISMISSED WITHOUT PREJUDICE. Plaintiff is granted 20 days to file an amended complaint.

IT IS SO ORDERED.

DATED: June 30, 2009.



LAWRENCE K. KARLTON
SENIOR JUDGE
UNITED STATES DISTRICT COURT