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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF CALIFORNIA

BRIDLEWOOD ESTATES PROPERTY OWNERS ASSOCIATION, a California Nonprofit Corporation,
Plaintiff,

v.

STATE FARM GENERAL INSURANCE COMPANY, an Illinois Corporation,
Defendant.

Case No.: 23-cv-00195-AJB-AHG

ORDER DENYING DEFENDANT’S MOTION TO DISMISS

(Doc. No. 9)

Before the Court is State Farm General Insurance Company’s (“Defendant” or “State Farm”) motion to dismiss Bridlewood Estates Property Owners Association’s (“Plaintiff” or “Bridlewood”) Complaint. (Doc. No. 9.) The motion is fully briefed. For the reasons set forth below, the Court **DENIES** Defendant’s motion.

I. BACKGROUND¹

Defendant insures Plaintiff under a Residential Community Association Policy (“Policy”). The Policy includes an endorsement, which provides liability coverage for the

¹ The following facts are taken from the FAC and assumed true for purposes of this motion. *See Cahill v. Liberty Mut. Ins. Co.*, 80 F.3d 336, 337–38 (9th Cir. 1996).

1 wrongful acts of Plaintiff's directors and officers. This action arises from Defendant's
2 denial of insurance coverage to Plaintiff.

3 On September 27, 2022, Plaintiff, received an invoice totaling \$123,617.00 from
4 Aztec Paving, Inc. ("Aztec") for asphalt repairs it conducted at Plaintiff's property. The
5 invoice was sent via email by Aztec's Project Manager, Jon Seethaler ("Seethaler"), from
6 his email address: jon@aztecpaving.com. Later that day, Plaintiff received an email
7 appearing to be from Seethaler, explaining that Aztec is moving away from receiving check
8 payments to direct electronic wire transfers. The sender's email address was
9 jon@aztecpavlng.com.

10 Plaintiff sent the invoice to its Treasurer, Owen Thomas ("Thomas"), for processing
11 and copied him to the email chain with Seethaler. On September 28, 2022, Thomas
12 received emails from Seethaler at his email address, jon@aztecpaving.com, informing him
13 of Aztec's move to a paperless system and that payment may be sent via wire transfer.
14 Thomas thereafter replied to Seethaler's email asking him to provide Aztec's wire transfer
15 information.

16 The next day, Thomas received an email from jon@aztecpavlng.com with an
17 attachment containing what appeared to be Aztec's wire transfer instructions. On October
18 3, 2022, Thomas wired \$123,617.00 from Plaintiff's bank account using the wire transfer
19 instructions provided.

20 Three days later, Seethaler emailed Thomas notifying him that Aztec has not yet
21 received the wire transfer. Plaintiff subsequently discovered that the wiring instructions
22 Thomas used to transmit payment to Aztec were sent by a fake email address,
23 jon@aztecpavlng.com. Plaintiff believes the communications between Thomas and the
24 fake email address occurred via hacking of Aztec's email server.

25 Between October and November 2022, Aztec demanded payment from Plaintiff and
26 filed a Mechanics Lien ("Aztec Lien") on its property. Plaintiff tendered the demand and
27 mechanics lien to Defendant, seeking coverage under the Policy's Directors and Officers
28 Liability Endorsement. On December 16, 2022, Defendant denied coverage, asserting that

1 Aztec’s claim against Plaintiff was not based on a wrongful act of an officer within the
2 meaning of the Policy, but rather, Plaintiff’s failure to pay a contractual obligation and debt
3 owed.

4 Later in December, Aztec’s subcontractor, Superior, filed a mechanics lien
5 (“Superior Lien”) against Plaintiff, and Aztec filed in San Diego Superior Court a
6 Complaint against Plaintiff alleging breach of contract and related claims (“Aztec
7 Complaint”).

8 On January 13, 2023, Plaintiff tendered the Aztec Lien and Superior Lien to
9 Defendant for defense and indemnification under the Policy. After being served with the
10 Aztec Complaint, Plaintiff tendered it to Defendant, demanding it agree to defend and
11 indemnify Plaintiff with respect to the Aztec Lien, Superior Lien, and Aztec Complaint.
12 Defendant denied coverage to Plaintiff for the mechanic liens, but has not responded to
13 Plaintiff’s tender of the Aztec Complaint.

14 According to Plaintiff, it attached to the tender letters the email chain showing the
15 wire instructions sent by the fake email address to Plaintiff and utilized by its Treasurer,
16 Thomas, to wire the \$123,617.00 payment to Aztec. Plaintiff alleges Defendant
17 unreasonably denied coverage by ignoring facts made known to them that would
18 potentially trigger coverage and placed its economic interests ahead of its insured.

19 Plaintiff filed the instant action against Defendant, alleging breach of contract,
20 breach of implied covenant and good faith and fair dealing, and declaratory relief. (Doc.
21 No. 1.) Defendant filed a motion to dismiss Plaintiff’s Complaint. (Doc. No. 9.) This Order
22 follows.

23 **II. LEGAL STANDARD**

24 A motion to dismiss pursuant to Federal Rule of Civil Procedure (“Rule”) 12(b)(6)
25 tests the legal sufficiency of the complaint. *Navarro v. Block*, 250 F.3d 729, 732 (9th Cir.
26 2001).² “To survive a motion to dismiss, a complaint must contain sufficient factual matter,
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28 ² Unless otherwise indicated, internal citations, quotation marks, and alterations are omitted from the case citations in this Order.

1 accepted as true, to ‘state a claim to relief that is plausible on its face.’” *Ashcroft v. Iqbal*,
2 556 U.S. 662, 678 (2009) (citation omitted). Facial plausibility is satisfied “when the
3 plaintiff pleads factual content that allows the court to draw the reasonable inference that
4 the defendant is liable for the misconduct alleged.” *Id.* To determine the sufficiency of the
5 complaint, the court must assume the truth of all factual allegations and construe them in
6 the light most favorable to the plaintiff. *Cahill v. Liberty Mut. Ins. Co.*, 80 F.3d 336, 337–
7 38 (9th Cir. 1996). Although a court must take all factual allegations in a complaint as true,
8 it is not required to accept conclusory statements. *Iqbal*, 556 U.S. at 678.

9 **III. DISCUSSION**

10 Defendant makes clear that disposition of its motion to dismiss turns on whether the
11 circumstances of Plaintiff’s case is covered under the Policy’s Directors and Officers
12 Liability Endorsement (“DO Endorsement”). Specifically, Defendant argues that Plaintiff
13 has not stated a claim for breach of the Policy because there was no wrongful act within
14 the meaning of the DO Endorsement to trigger its duty to defend and indemnify. The Court
15 disagrees.

16 **A. California Liability Insurance Law³**

17 Under California law, liability insurance generally “imposes two separate
18 obligations on the insurer: (1) to indemnify its insured against third party claims covered
19 by the policy (by settling the claim or paying any judgment against the insured); and (2) to
20 defend such claims against its insured (by furnishing competent counsel and paying
21 attorney fees and costs.” *Howard v. Am. Nat’l Fire Ins. Co.*, 115 Cal. Rptr. 3d 42, 61 (Ct.
22 App. 2010). “Although correlative, the duty to indemnify and the duty to defend are not
23 coterminous.” *Certain Underwriters at Lloyd’s of London v. Superior Ct.*, 24 Cal. 4th 945,
24 958 (2001). While the duty to defend may arise as soon as damages are sought in some
25 amount, the duty to indemnify can arise only after damages are fixed in their amount. *Id.*

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³ There is no dispute that California law applies.

1 In turn, “[w]here there is a duty to defend, there may be a duty to indemnify; but where
2 there is no duty to defend, there cannot be a duty to indemnify.” *Id.*

3 “[A] liability insurer owes a broad duty to defend its insured against claims that
4 create a potential for indemnity.” *Horace Mann Ins. Co. v. Barbara B.*, 4 Cal. 4th 1076,
5 1081 (1993). The insured bears the initial burden “to prove that an event is a claim within
6 the scope of the basic coverage.” *Royal Globe Ins. Co. v. Whitaker*, 226 Cal. Rptr. 435, 437
7 (Ct. App. 1986). Once established, the burden shifts to the insurer “to prove a claim covered
8 falls within an exclusion.” *Id.* As such, “[t]o prevail, the insured must prove the existence
9 of a *potential for coverage*, while the insurer must establish *the absence of any such*
10 *potential.*” *Montrose Chem. Corp. v. Superior Ct.*, 6 Cal. 4th 287, 300 (1993) (emphasis in
11 original).

12 Where a third-party claim is involved, “the test is whether the underlying action for
13 which defense and indemnity is sought potentially seeks relief within the coverage of the
14 policy.” *La Jolla Beach & Tennis Club, Inc. v. Industrial Indemnity Co.*, 9 Cal. 4th 27, 44
15 (1994) (emphasis omitted). An insurer must therefore “defend against a suit even where
16 the evidence suggests but does not conclusively establish that the loss is not covered.”
17 *Hartford Cas. Ins. Co. v. Swift Distribution, Inc.*, 59 Cal. 4th 277, 286 (2014).
18 “Determination of the duty to defend depends, in the first instance, on a comparison
19 between the allegations of the complaint and the terms of the policy.” *Id.* at 287. The duty
20 is also triggered “where extrinsic facts known to the insurer suggest that the claim may be
21 covered.” *Id.* As such, “[i]f any facts stated or fairly inferable in the complaint, or otherwise
22 known or discovered by the insurer, suggest a claim potentially covered by the policy, the
23 insurer’s duty to defend arises and is not extinguished until the insurer negates all facts
24 suggesting potential coverage.” *Id.* Generally, “doubt as to whether an insurer owes a duty
25 to defend must be resolved in favor of the insured.” *Id.*

26 In determining whether a claim creates the potential for coverage under an insurance
27 policy, statutory rules of contract interpretation apply. *Id.* at 288. Thus, “the mutual
28 intention of the parties at the time the contract is formed governs interpretation.” *Id.* To

1 determine intent, the court looks “first to the language of the contract in order to ascertain
2 its plain meaning or the meaning a layperson would ordinarily attach to it.” *Id.* The court
3 “must also interpret the language in context, with regard to its intended function in the
4 policy.” *Id.*

5 **B. Wrongful Act Within the Meaning of the DO Endorsement**

6 Plaintiff’s causes of action for breach of contract, breach of the implied covenant of
7 good faith and fair dealing, and declaratory relief are all predicated on its allegations that
8 State Farm wrongfully failed to provide defense and/or indemnity under the Policy in
9 connection with the Aztec Lien, the Superior Lien, and the Aztec Complaint.

10 Pertinent here, the Policy’s DO Endorsement states that State Farm “will pay those
11 sums that the insured becomes legally obligated to pay as damages because of a ‘wrongful
12 act’ to which this endorsement applies.” (Doc. No. 1-3 at 18.) According to the DO
13 Endorsement:

14 “Wrongful act” means any actual or alleged error, misstatement, misleading
15 statement, act, omission, neglect, or breach of duty committed, attempted or
16 allegedly committed or attempted by an insured arising solely out, of his or
17 her capacity as director, officer “manager” or trustee relating to the operations
18 of your organization.

19 (Doc. No. 1-3 at 20.)

20 As to whether Plaintiff has carried its initial burden that the claim is potentially
21 covered under the Policy, the Court finds it has. Comparing the allegations in the Aztec
22 Complaint and the terms of the DO Endorsement, the Court does not find that Aztec’s
23 breach of contract claim is necessarily disqualified from coverage. According to Aztec,
24 Plaintiff breached its contract with Aztec “by failing and refusing, without just cause or
25 excuse, to pay” for services it rendered. (Doc. No. 1-14 at 4.) The DO Endorsement does
26 not expressly exclude contractual liabilities from coverage. Indeed, it delineates nineteen
27 different exclusions; none are for contractual violations. (Doc. No. 1-3 at 18–20.)
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1 Moreover, Plaintiff has presented extrinsic facts known to State Farm which suggest
2 a potential claim for coverage based on the Treasurer’s error, negligence, or breach of duty.
3 *See Hartford Cas. Ins. Co.*, 59 Cal. 4th at 287 (“duty [to defend] also exists where extrinsic
4 facts known to the insurer suggest that the claim may be covered.”). State Farm is aware
5 of facts supporting Plaintiff’s claim that its Treasurer processed the \$123,617.00 payment
6 for Aztec’s invoice, “but payment was misdirected due to hacking of the contractor’s email
7 system, causing the officer of Bridlewood to wire payment into the hacker’s bank account.”
8 (Doc. No. 1 at 3.) Specifically, State Farm is in possession of the email communications
9 showing the deception that led to the Treasurer’s payment error. (*Id.* at 11; Doc. No. 1-5 at
10 2–10.)

11 State Farm is also aware of Plaintiff’s and Aztec’s discovery exchanges in the
12 underlying action, which show that Plaintiff raised with Aztec, as a possible defense, its
13 Treasurer’s payment to a bank account he believed belonged to Aztec. (Doc. No. 13-2 at
14 5.) Aztec responded that it did not receive that payment because Plaintiff’s Treasurer sent
15 the payment to a bank account that did not belong to Aztec. (*Id.* at 5, 7.) In further support
16 of its contention that it did not receive payment, Aztec explained that Plaintiff’s Treasurer
17 “wired funds to a bank account that was provided to him in an email, with an address that
18 was not previously used to communicate with Estimator/Project Manager, Jon Seethaler.
19 The email address did not use the same domain name as the email address used by
20 Estimator/Project Manager, Jon Seethaler.” (*Id.* at 11.) Aztec also faults Plaintiff’s
21 Treasurer for not contacting Aztec to confirm the wiring instructions prior to transferring
22 the funds. (*Id.*)

23 The Court finds the foregoing extrinsic evidence suggests a potential for coverage
24 under the DO Endorsement because they support a finding that Plaintiff’s Treasurer
25 committed a “wrongful act” when he transmitted payment of Aztec’s invoice to the wrong
26 bank account, which in turn, gave rise to the Aztec Complaint. Had it not been for the
27 Treasurer’s mistake, Aztec would have received payment and have no cause to sue
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1 Plaintiff. As such, Defendant’s attempt to cast the Treasurer’s payment error as irrelevant
2 to the breach of contract claim is unavailing.

3 Defendant also argues that California law is well settled that an insured’s failure to
4 pay amounts due under a contract does not qualify as a wrongful act. In support, Defendant
5 cites *Aug. Ent., Inc. v. Philadelphia Indem. Ins. Co.*, and similar cases where “a corporation
6 intentionally entered into a contract, decided not to make payment on it, and looked to its
7 D & O insurer for a bailout.” 52 Cal. Rptr. 3d 908, 915 (Ct. App. 2007). This case is
8 different.

9 This is not a case where an insured simply refused to pay amounts due under a
10 contract. As previously discussed, Plaintiff did pay the \$123,617.00 that Aztec invoiced.
11 Due to its Treasurer’s error, however, the payment was sent to a hacker. Had Plaintiff’s
12 Treasurer not been deceived by the hacker’s communication, Aztec would have received
13 the \$123,617.00 and Plaintiff would not be liable for the loss of another \$123,617.00 plus
14 fees and interest. Because the instant case is not one where a plaintiff is merely attempting
15 to pass on its contractual obligations to its insurer, the Court does not find it falls within
16 the purview of California case law finding that failure to pay amounts due under a contract
17 does constitute a wrongful act for purposes of directors and liability coverage.

18 Albeit unpublished, the Court finds the Ninth Circuit’s ruling in *Erickson-Hall*
19 *Constr. Co. v. Hartford Fire Ins. Co.*, 800 F. App’x 559 (9th Cir. 2020) persuasive and
20 instructive. There, the court pointed out that “under California law, an insured’s losses for
21 breach of contract are not uninsurable as a matter of law.” *Id.* at 560. As such, to the extent
22 Defendant argues that losses from a breach of contract are per se not covered by insurance,
23 the argument is without merit. “Rather, the nature of the damage and the risk involved, in
24 light of particular policy provisions, control coverage” in a particular case. *See id.* (quoting
25 *Vandenberg v. Superior Court*, 21 Cal.4th 815, 839 (1999)). Applying this framework, the
26 Ninth Circuit looked at the language of the policy at issue and the allegations in the
27 plaintiff’s complaint to determine whether the nature of the damage and risk the plaintiff
28 sought to cover “was exactly that which did in fact transpire.” *Id.* at 560.

1 The case involved an employer who obtained fiduciary liability insurance coverage
2 to cover risks of loss arising from potential mistakes in administering employee benefits
3 plans. The complaint alleged that the employer’s controller failed to counsel employees
4 that their benefits plans had lapsed due to nonpayment of premiums. The controller also
5 mishandled documents relating to the plans, including failing to receive and process
6 premium invoices, deduct premium amounts from employees’ paychecks, and paying
7 premiums on behalf of the employer and its employees. Because the fiduciary liability
8 insurance covers an error or omission in the administration of the benefits plans resulting
9 in a loss, and the complaint’s allegations demonstrated facts showing that the benefits plans
10 were indeed negligently administered, resulting in the employer’s loss, the Ninth Circuit
11 found that the employer’s claimed losses were not (as the district court found and
12 Defendant here contends) amounts it was obligated to pay its employees by contract,
13 independent of any wrongful act. *Id* at 559, 560. Indeed, the court emphasized that “*but for*
14 the allegedly negligent acts of Erickson-Hall’s Controller, the premiums would have been
15 paid . . .” and “Erickson-Hall would never have been liable for the claimed loss amounts.”
16 *Id.* at 560 (emphasis in original).

17 The same is true here. The Policy’s DO Endorsement states that State Farm will
18 provide coverage for “sums that the insured becomes legally obligated to pay as damages
19 because of a ‘wrongful act.’” (Doc. No. 1-3 at 18.) A wrongful act includes any “error . . .
20 act, omission, neglect, or breach of duty” committed by an insured “arising solely out, of
21 his or her capacity as director, officer ‘manager’ or trustee relating to the operations of your
22 organization.” (*Id.* at 20.) Plaintiff’s Complaint alleges that its Treasurer, an officer of its
23 organization, wired Aztec’s payment to a hacker’s bank account by “failing to verify with
24 proper diligence the proper wiring instruction to wire the payment.” (Doc. No. 1 at 9.)
25 These allegations show that the Treasurer committed an error, omission, neglect, or breach
26 of duty arising out of his official capacity to process payments for Bridlewood. As such,
27 the nature of the damage and risk the DO Endorsement covers is “exactly that which did
28 in fact transpire.” *Erickson-Hall Constr. Co.*, 800 F. App’x at 560.

1 The Court agrees with Plaintiff that to the extent liability is found in the Aztec action,
2 the basis of liability would be the Treasurer’s alleged wrongful act, triggering coverage.
3 Like in *Erickson-Hall*, but for the Treasurer’s negligent acts, Aztec’s payment would not
4 have been misdirected into a hacker’s account, Aztec would have received the payment,
5 and Plaintiff would not have incurred the claimed losses.


6 Based on the foregoing, the Court finds that Plaintiff has shown that its claimed loss
7 falls within the basic scope of coverage.⁴ *See Hartford Cas. Ins. Co.*, 59 Cal. 4th at 288
8 (“the insured need only show that the underlying claim *may* fall within policy coverage;
9 the insurer must prove it *cannot*.” (emphasis in original)). And because Defendant does not
10 argue that any policy exclusion bars coverage, it cannot meet its burden to conclusively
11 establish that the loss is not covered. *See id.* at 287 (“An insurer must defend against a suit
12 even where the evidence suggests, but does not conclusively establish, that the loss is not
13 covered.”). Accordingly, the Court denies Defendant’s motion to dismiss.

14 **IV. CONCLUSION**

15 For the reasons stated herein, Defendant’s motion to dismiss is **DENIED**. Defendant
16 must file an answer to the Complaint no later than April 1, 2024.

17 **IT IS SO ORDERED.**

18 Dated: March 18, 2024

19 
20 Hon. Anthony J. Battaglia
21 United States District Judge
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27 _____
28 ⁴ At the very least, the instant case presents a close call, and generally, “doubt as to whether an insurer
owes a duty to defend must be resolved in favor of the insured.” *Hartford Cas. Ins. Co.*, 59 Cal. 4th at
287.