Docket #3854 Date Filed: 12/24/2019

Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com

Abigail V. O'Brient (SBN 265704)
MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3200
Email: avobrient@mintz.com

*Attorneys for UMB Bank, National Association| and Wells Fargo Bank, National Association as Trustees*

[additional counsel on next page]

**UNITED STATES BANKRUPTCY COURT**
**CENTRAL DISTRICT OF CALIFORNIA – LOS ANGELES DIVISION**

In re:

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

Debtors and Debtors In Possession.

☒ Affects All Debtors
☐ Affects Verity Health System of California, Inc.
☐ Affects O'Connor Hospital
☐ Affects Saint Louise Regional Hospital
☐ Affects St. Francis Medical Center
☐ Affects St. Vincent Medical Center
☐ Affects Seton Medical Center
☐ Affects O'Connor Hospital Foundation
☐ Affects Saint Louise Regional Hospital Foundation
☐ Affects St. Francis Medical Center of Lynwood Foundation
☐ Affects St. Vincent Foundation
☐ Affects St. Vincent Dialysis Center, Inc.
☐ Affects Seton Medical Center Foundation
☐ Affects Verity Business Services
☐ Affects Verity Medical Foundation
☐ Affects Verity Holdings, LLC
☐ Affects De Paul Ventures, LLC
☐ Affects De Paul Ventures - San Jose Dialysis, LLC

Debtors and Debtors In Possession.

Lead Case No. 2:18-bk-20151-ER

Jointly Administered With:

CASE NO.: 2:18-bk-20162-ER
CASE NO.: 2:18-bk-20163-ER
CASE NO.: 2:18-bk-20164-ER
CASE NO.: 2:18-bk-20165-ER
CASE NO.: 2:18-bk-20167-ER
CASE NO.: 2:18-bk-20168-ER
CASE NO.: 2:18-bk-20169-ER
CASE NO.: 2:18-bk-20171-ER
CASE NO.: 2:18-bk-20172-ER
CASE NO.: 2:18-bk-20173-ER
CASE NO.: 2:18-bk-20175-ER
CASE NO.: 2:18-bk-20176-ER
CASE NO.: 2:18-bk-20178-ER
CASE NO.: 2:18-bk-20179-ER
CASE NO.: 2:18-bk-20180-ER
CASE NO.: 2:18-bk-20181-ER

Chapter 11 Cases

Hon. Judge Ernest M. Robles

**JOINT RESPONSE OF UMB BANK, N.A., WELLS FARGO BANK, NATIONAL ASSOCIATION, AND U.S. BANK, NATIONAL ASSOCIATION TO COMMITTEE'S OMNIBUS CLAIM OBJECTION**

**[RELATED TO DOCKET NO. 3634]**

**Hearing Date: January 7, 2020**
**Time: 10:00 a.m.**
**Location: Courtroom 1568**

1820151191224000000000003

Jason D. Strabo (SBN 246426)
MCDERMOTT WILL & EMERY LLP
2049 Century Park East, 38th Floor
Minneapolis, MN 55402
Tel: 310-788-4125
Fax: 310-277-4730
Email: jstrabo@mwe.com

Jason M. Reed (admitted pro hac vice)
MASLON LLP
90 South Seventh Street, Suite 3300
Minneapolis, MN 55402
Tel: 612-672-8200
Fax: 612-642-8301
Email: Jason.Reed@maslon.com

Nathan F. Coco (admitted pro hac vice)
Megan Preusker (admitted pro hac vice)
MCDERMOTT WILL & EMERY LLP
444 West Lake Street, Suite 4000
Chicago, IL 60606-0029
Tel: 312-327-2000
Fax: 312-984-7700
Email: ncoco@mwe.com
Email: mpreusker@mwe.com

*Attorneys for U.S. Bank National Association*

*Attorneys for U.S. Bank National Association*

UMB Bank, N.A., as successor master indenture trustee for the master indenture obligations ("UMB"), Wells Fargo Bank, National Association, as indenture trustee for the series 2005 revenue bonds ("Wells Fargo"), and U.S. Bank, National Association, as indenture trustee for both the 2015 notes and the 2017 notes ("US Bank," and together with UMB and Wells Fargo, the "Trustees"), hereby file this response (the "Response") to the *Official Committee of Unsecured Creditors' Omnibus Objection to Claims Filed by U.S. Bank National Association, UMB Bank, N.A., and Wells Fargo Bank, National Association, as Trustees; Declaration of Mark Shinderman in Support Thereof*, dated November 18, 2019 [Docket No. 3634] (the "Omnibus Claim Objection") filed by the Official Committee of Unsecured Creditors of Verity Health System of California, Inc., *et al.* (the "Committee"), and in support hereof, respectfully state as follows:

**RESPONSE**

The relief sought by the Committee pursuant to the Omnibus Claim Objection is duplicative of, and wholly dependent upon, the relief sought by the Committee pursuant to the Adversary Actions (as defined in the Omnibus Claims Objection) against UMB and US Bank in Adversary Proceeding Nos. 2:19-ap-19-01166-ER and 2:19-ap-19-01165-ER, respectively. In

fact, the Committee states clearly that it "objects to the claims identified in the chart below on the bases set forth in the Adversary Actions." Omnibus Claim Objection at 2. The Committee's support for the Omnibus Claim Objection is solely comprised of the First Amended Complaints filed by the Committee in the Adversary Actions, which the Committee attaches as exhibits to the Omnibus Claim Objection.

The Trustees assert that, due to the entirely duplicative nature of the Adversary Actions and the Omnibus Claim Objection, it is unnecessary and wasteful for the parties to litigate both the Adversary Actions and the Omnibus Claim Objection on separate tracks. Rather, because any decision or resolution of the Adversary Actions will likely determine the resolution of the Omnibus Claim Objection, the Omnibus Claim Objection should be held in abeyance pending any decision or resolution of the Adversary Actions, or further order of the Court.

In support of this Response, attached hereto as Exhibit A is the Motion to Dismiss the First Amended Complaint filed by UMB on September 30, 2019 [Adv. Docket No. 37] (the "UMB Motion to Dismiss"), as well as UMB's reply to the Committee's opposition to the UMB Motion to Dismiss filed on October 24, 2019 [Adv. Docket No. 44]. Attached hereto as Exhibit B is the Motion to Dismiss the First Amended Complaint filed by US Bank on September 30, 2019 [Adv. Docket No. 39] (the "US Bank Motion to Dismiss"), as well as US Bank's reply to the Committee's opposition to the US Bank Motion to Dismiss filed on October 24, 2019 [Adv. Docket No. 44]. The Trustees incorporate such exhibits by reference as if fully set forth herein.

A hearing on the Omnibus Claim Objection is scheduled for January 7, 2020 (the "Claim Objection Hearing"). The hearing regarding the UMB Motion to Dismiss and the US Bank Motion to Dismiss is currently scheduled for January 8, 2020 [Adv. Dockets Nos. 50]. In light of the duplicative nature of the Adversary Actions and the Omnibus Claim Objection, the Trustees submit that it would be appropriate and in the best interest of judicial economy to generally adjourn all deadlines associated with the Omnibus Claim Objection, including the Claim Objection Hearing, and to hold the Omnibus Claim Objection in abeyance pending decision or resolution of the Adversary Actions, or further order of the Court.

## CONCLUSION

**WHEREAS,** for the foregoing reasons, the Trustees respectfully request that this Court (i) generally adjourn all deadlines associated with the Omnibus Claim Objection, including the Claim Objection Hearing, pending further order of the Court, (ii) hold the Omnibus Claim Objection in abeyance pending decision or resolution of the Adversary Actions, or further order of the Court, and (iii) grant the Trustees such other and further relief as is just and proper.

.

DATED: December 24, 2019

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.

/s/ Abigail V. O'Brient

Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

-and-

Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3200
Email: avobrient@mintz.com

*Attorneys for UMB Bank, N.A. as master indenture trustee and Wells Fargo, National Association, as indenture trustee*

DATED: December 24, 2019

MCDERMOTT WILL & EMERY LLP

Jason D. Strabo (SBN 246426)
2049 Century Park East, 38th Floor
Minneapolis, MN 55402
Tel: 310-788-4125
Fax: 310-277-4730
Email: jstrabo@mwe.com

## CONCLUSION

**WHEREAS,** for the foregoing reasons, the Trustees respectfully request that this Court (i) generally adjourn all deadlines associated with the Omnibus Claim Objection, including the Claim Objection Hearing, pending further order of the Court, (ii) hold the Omnibus Claim Objection in abeyance pending decision or resolution of the Adversary Actions, or further order of the Court, and (iii) grant the Trustees such other and further relief as is just and proper.

DATED: December 24, 2019

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.

Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

-and-

Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3200
Email: avobrient@mintz.com

*Attorneys for UMB Bank, N.A. as master indenture trustee and Wells Fargo, National Association, as indenture trustee*

DATED: December 24, 2019

MCDERMOTT WILL & EMERY LLP

Megan Preusker

Jason D. Strabo (SBN 246426)
2049 Century Park East, 38th Floor
Minneapolis, MN 55402
Tel: 310-788-4125
Fax: 310-277-4730
Email: jstrabo@mwe.com

-and-

Nathan F. Coco (admitted pro hac vice)
Megan Preusker (admitted pro hac vice)
MCDERMOTT WILL & EMERY LLP
444 West Lake Street, Suite 4000
Chicago, IL 60606-0029
Tel: 312-327-2000
Fax: 312-984-7700
Email: ncoco@mwe.com
Email: mpreusker@mwe.com

*Attorneys for U.S. Bank National Association, not individually but as Series 2015 Note Trustee*

DATED: December 24, 2019

MASLON LLP

Jason M. Reed (admitted pro hac vice)
90 South Seventh Street, Suite 3300
Minneapolis, MN 55402
Tel: 612-672-8200
Fax: 612-642-8301
Email: Jason.Reed@maslon.com

*Attorneys for U.S. Bank National Association, not individually but as Series 2017 Note Trustee*

# PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is: 2029 Century Park East, Suite 3100, Los Angeles, CA 90067

A true and correct copy of the foregoing document entitled (*specify*): **JOINT RESPONSE OF UMB BANK, N.A., WELLS FARGO BANK, NATIONAL ASSOCIATION, AND U.S. BANK, NATIONAL ASSOCIATION TO COMMITTEE'S OMNIBUS CLAIM OBJECTION** will be served or was served **(a)** on the judge in chambers in the form and manner required by LBR 5005-2(d); and **(b)** in the manner stated below:

**1**. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**: Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On (*date*) December 24, 2019, I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

☒ Service information continued on attached page

**2. SERVED BY UNITED STATES MAIL**:
On (*date*) _____, I served the following persons and/or entities at the last known addresses in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

☐ Service information continued on attached page

**3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL** (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on (*date*) December 24, 2019, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

| | |
|---|---|
| **VIA FEDERAL EXPRESS**:<br>Honorable Ernest Robles<br>U.S. Bankruptcy Court<br>Roybal Federal Building<br>255 E. Temple Street, Suite 1560<br>Los Angeles, CA 90012 | |

☒ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

| December 24, 2019 | Diane Hashimoto | /s/ Diane Hashimoto |
|---|---|---|
| *Date* | *Printed Name* | *Signature* |

**NEF SERVICE LIST**

- Alexandra Achamallah aachamallah@milbank.com, rliubicic@milbank.com
- Melinda Alonzo ml7829@att.com
- Robert N Amkraut ramkraut@foxrothschild.com
- Kyra E Andrassy kandrassy@swelawfirm.com, lgarrett@swelawfirm.com;gcruz@swelawfirm.com;jchung@swelawfirm.com
- Simon Aron saron@wrslawyers.com
- Lauren T Attard lattard@bakerlaw.com, agrosso@bakerlaw.com
- Allison R Axenrod allison@claimsrecoveryllc.com
- Cristina E Bautista cristina.bautista@kattenlaw.com, ecf.lax.docket@kattenlaw.com
- James Cornell Behrens jbehrens@milbank.com, gbray@milbank.com;mshinderman@milbank.com;dodonnell@milbank.com;jbrewster@milbank.com;JWeber@milbank.com
- Ron Bender rb@lnbyb.com
- Bruce Bennett bbennett@jonesday.com
- Peter J Benvenutti pbenvenutti@kellerbenvenutti.com, pjbenven74@yahoo.com
- Leslie A Berkoff lberkoff@moritthock.com, hmay@moritthock.com
- Steven M Berman sberman@slk-law.com
- Stephen F Biegenzahn efile@sfblaw.com
- Karl E Block kblock@loeb.com, jvazquez@loeb.com;ladocket@loeb.com;kblock@ecf.courtdrive.com
- Dustin P Branch branchd@ballardspahr.com, carolod@ballardspahr.com;hubenb@ballardspahr.com
- Michael D Breslauer mbreslauer@swsslaw.com, wyones@swsslaw.com;mbreslauer@ecf.courtdrive.com;wyones@ecf.courtdrive.com
- Chane Buck cbuck@jonesday.com
- Lori A Butler butler.lori@pbgc.gov, efile@pbgc.gov
- Howard Camhi hcamhi@ecjlaw.com, tcastelli@ecjlaw.com;amatsuoka@ecjlaw.com
- Barry A Chatz barry.chatz@saul.com, jurate.medziak@saul.com
- Shirley Cho scho@pszjlaw.com
- Shawn M Christianson cmcintire@buchalter.com, schristianson@buchalter.com
- Louis J. Cisz lcisz@nixonpeabody.com, jzic@nixonpeabody.com
- Leslie A Cohen leslie@lesliecohenlaw.com, jaime@lesliecohenlaw.com;olivia@lesliecohenlaw.com
- Marcus Colabianchi mcolabianchi@duanemorris.com
- Kevin Collins kevin.collins@btlaw.com, Kathleen.lytle@btlaw.com
- Joseph Corrigan Bankruptcy2@ironmountain.com
- David N Crapo dcrapo@gibbonslaw.com, elrosen@gibbonslaw.com
- Mariam Danielyan md@danielyanlawoffice.com, danielyan.mar@gmail.com
- Brian L Davidoff bdavidoff@greenbergglusker.com, calendar@greenbergglusker.com;jking@greenbergglusker.com
- Aaron Davis aaron.davis@bryancave.com, kat.flaherty@bryancave.com
- Lauren A Deeb lauren.deeb@nelsonmullins.com, maria.domingo@nelsonmullins.com
- Daniel Denny ddenny@milbank.com
- Anthony Dutra adutra@hansonbridgett.com
- Kevin M Eckhardt kevin.eckhardt@gmail.com, keckhardt@hunton.com
- Lei Lei Wang Ekvall lekvall@swelawfirm.com, lgarrett@swelawfirm.com;gcruz@swelawfirm.com;jchung@swelawfirm.com
- David K Eldan david.eldan@doj.ca.gov, teresa.depaz@doj.ca.gov
- Andy J Epstein taxcpaesq@gmail.com
- Richard W Esterkin richard.esterkin@morganlewis.com
- Christine R Etheridge christine.etheridge@ikonfin.com

**NEF SERVICE LIST**

- M Douglas Flahaut flahaut.douglas@arentfox.com
- Michael G Fletcher mfletcher@frandzel.com, sking@frandzel.com
- Joseph D Frank jfrank@fgllp.com, mmatlock@fgllp.com;csmith@fgllp.com;jkleinman@fgllp.com;csucic@fgllp.com
- William B Freeman bill.freeman@kattenlaw.com, nicole.jones@kattenlaw.com,ecf.lax.docket@kattenlaw.com
- John-Patrick M Fritz jpf@lnbyb.com, JPF.LNBYB@ecf.inforuptcy.com
- Eric J Fromme efromme@tocounsel.com, lchapman@tocounsel.com;sschuster@tocounsel.com
- Amir Gamliel amir-gamliel-9554@ecf.pacerpro.com, cmallahi@perkinscoie.com;DocketLA@perkinscoie.com
- Jeffrey K Garfinkle jgarfinkle@buchalter.com, docket@buchalter.com;dcyrankowski@buchalter.com
- Thomas M Geher tmg@jmbm.com, bt@jmbm.com;fc3@jmbm.com;tmg@ecf.inforuptcy.com
- Lawrence B Gill lgill@nelsonhardiman.com, rrange@nelsonhardiman.com;mmarkwell@nelsonhardiman.com
- Paul R. Glassman pglassman@sycr.com
- Matthew A Gold courts@argopartners.net
- Eric D Goldberg eric.goldberg@dlapiper.com, eric-goldberg-1103@ecf.pacerpro.com
- Marshall F Goldberg mgoldberg@glassgoldberg.com, jbailey@glassgoldberg.com
- Richard H Golubow rgolubow@wcghlaw.com, pj@wcghlaw.com;jmartinez@wcghlaw.com;Meir@virtualparalegalservices.com
- David M. Guess guessd@gtlaw.com
- Anna Gumport agumport@sidley.com
- Melissa T Harris harris.melissa@pbgc.gov, efile@pbgc.gov
- James A Hayes jhayes@zinserhayes.com, jhayes@jamesahayesaplc.com
- Michael S Held mheld@jw.com
- Lawrence J Hilton lhilton@onellp.com, lthomas@onellp.com,info@onellp.com,rgolder@onellp.com,lhyska@onellp.com,nlichtenberger@onellp.com
- Robert M Hirsh Robert.Hirsh@arentfox.com
- Florice Hoffman fhoffman@socal.rr.com, floricehoffman@gmail.com
- Lee F Hoffman leehoffmanjd@gmail.com, lee@fademlaw.com
- Michael Hogue hoguem@gtlaw.com, SFOLitDock@gtlaw.com;navarrom@gtlaw.com
- Matthew B Holbrook mholbrook@sheppardmullin.com, mmanns@sheppardmullin.com
- David I Horowitz david.horowitz@kirkland.com, keith.catuara@kirkland.com;terry.ellis@kirkland.com;elsa.banuelos@kirkland.com;ivon.granados@kirkland.com
- Brian D Huben hubenb@ballardspahr.com, carolod@ballardspahr.com
- Joan Huh joan.huh@cdtfa.ca.gov
- Benjamin Ikuta bikuta@hml.law
- Lawrence A Jacobson laj@cohenandjacobson.com
- John Mark Jennings johnmark.jennings@kutakrock.com, mary.clark@kutakrock.com
- Monique D Jewett-Brewster mjb@hopkinscarley.com, eamaro@hopkinscarley.com
- Crystal Johnson M46380@ATT.COM
- Gregory R Jones gjones@mwe.com, rnhunter@mwe.com
- Jeff D Kahane jkahane@duanemorris.com, dmartinez@duanemorris.com
- Steven J Kahn skahn@pszyjw.com
- Cameo M Kaisler salembier.cameo@pbgc.gov, efile@pbgc.gov
- Ivan L Kallick ikallick@manatt.com, ihernandez@manatt.com
- Ori Katz okatz@sheppardmullin.com, cshulman@sheppardmullin.com;ezisholtz@sheppardmullin.com;lsegura@sheppardmullin.com
- Payam Khodadadi pkhodadadi@mcguirewoods.com, dkiker@mcguirewoods.com
- Christian T Kim ckim@dumas-law.com, ckim@ecf.inforuptcy.com
- Jane Kim jkim@kellerbenvenutti.com

**NEF SERVICE LIST**

- Monica Y Kim myk@lnbrb.com, myk@ecf.inforuptcy.com
- Gary E Klausner gek@lnbyb.com
- David A Klein david.klein@kirkland.com
- Nicholas A Koffroth nick.koffroth@dentons.com, chris.omeara@dentons.com
- Joseph A Kohanski jkohanski@bushgottlieb.com, kprestegard@bushgottlieb.com
- Jeffrey S Kwong jsk@lnbyb.com, jsk@ecf.inforuptcy.com
- Darryl S Laddin bkrfilings@agg.com
- Robert S Lampl advocate45@aol.com, rlisarobinsonr@aol.com
- Richard A Lapping richard@lappinglegal.com
- Paul J Laurin plaurin@btlaw.com, slmoore@btlaw.com;jboustani@btlaw.com
- Nathaniel M Leeds nathaniel@mitchelllawsf.com, sam@mitchelllawsf.com
- David E Lemke david.lemke@wallerlaw.com, chris.cronk@wallerlaw.com;Melissa.jones@wallerlaw.com;cathy.thomas@wallerlaw.com
- Lisa Lenherr llenherr@wendel.com, bankruptcy@wendel.com
- Elan S Levey elan.levey@usdoj.gov, louisa.lin@usdoj.gov
- Tracy L Mainguy bankruptcycourtnotices@unioncounsel.net, tmainguy@unioncounsel.net
- Samuel R Maizel samuel.maizel@dentons.com, alicia.aguilar@dentons.com;docket.general.lit.LOS@dentons.com;tania.moyron@dentons.com;kathryn.howard@dentons.com;joan.mack@dentons.com;derry.kalve@dentons.com
- Alvin Mar alvin.mar@usdoj.gov, dare.law@usdoj.gov
- Craig G Margulies Craig@MarguliesFaithlaw.com, Victoria@MarguliesFaithlaw.com;Helen@MarguliesFaithlaw.com
- Hutchison B Meltzer hutchison.meltzer@doj.ca.gov, Alicia.Berry@doj.ca.gov
- John J Menchaca (TR) jmenchaca@menchacacpa.com, ca87@ecfcbis.com;igaeta@menchacacpa.com
- Christopher Minier becky@ringstadlaw.com, arlene@ringstadlaw.com
- John A Moe john.moe@dentons.com, glenda.spratt@dentons.com
- Susan I Montgomery susan@simontgomerylaw.com, assistant@simontgomerylaw.com;simontgomerylawecf.com@gmail.com;montgomerysr71631@notify.bestcase.com
- Monserrat Morales Monsi@MarguliesFaithLaw.com, Victoria@MarguliesFaithLaw.com;Helen@marguliesfaithlaw.com
- Kevin H Morse kmorse@clarkhill.com, blambert@clarkhill.com
- Marianne S Mortimer mmartin@jmbm.com
- Tania M Moyron tania.moyron@dentons.com, chris.omeara@dentons.com;nick.koffroth@dentons.com
- Alan I Nahmias anahmias@mbnlawyers.com, jdale@mbnlawyers.com
- Akop J Nalbandyan jnalbandyan@LNtriallawyers.com, cbautista@LNtriallawyers.com
- Jennifer L Nassiri jennifernassiri@quinnemanuel.com
- Charles E Nelson nelsonc@ballardspahr.com, wassweilerw@ballardspahr.com
- Sheila Gropper Nelson shedoesbklaw@aol.com
- Mark A Neubauer mneubauer@carltonfields.com, mlrodriguez@carltonfields.com;smcloughlin@carltonfields.com;schau@carltonfields.com;NDunn@carltonfields.com;ecfla@carltonfields.com
- Fred Neufeld fneufeld@sycr.com, tingman@sycr.com
- Nancy Newman nnewman@hansonbridgett.com, ajackson@hansonbridgett.com;calendarclerk@hansonbridgett.com
- Bryan L Ngo bngo@fortislaw.com, BNgo@bluecapitallaw.com;SPicariello@fortislaw.com;JNguyen@fortislaw.com;JNguyen@bluecapitallaw.com
- Abigail V O'Brient avobrient@mintz.com, docketing@mintz.com;DEHashimoto@mintz.com;nleali@mintz.com;ABLevin@mintz.com;GJLeon@mintz.com

**NEF SERVICE LIST**

- John R OKeefe jokeefe@metzlewis.com, slohr@metzlewis.com
- Scott H Olson solson@vedderprice.com, jcano@vedderprice.com,jparker@vedderprice.com;scott-olson-2161@ecf.pacerpro.com,ecfsfdocket@vedderprice.com
- Giovanni Orantes go@gobklaw.com, gorantes@orantes-law.com,cmh@gobklaw.com,gobklaw@gmail.com,go@ecf.inforuptcy.com;orantesgr89122@notify.bestcase.com
- Keith C Owens kowens@venable.com, khoang@venable.com
- R Gibson Pagter gibson@ppilawyers.com, ecf@ppilawyers.com;pagterrr51779@notify.bestcase.com
- Paul J Pascuzzi ppascuzzi@ffwplaw.com
- Lisa M Peters lisa.peters@kutakrock.com, marybeth.brukner@kutakrock.com
- Christopher J Petersen cjpetersen@blankrome.com, gsolis@blankrome.com
- Mark D Plevin mplevin@crowell.com, cromo@crowell.com
- Steven G. Polard spolard@ch-law.com, calendar-lao@rmkb.com;melissa.tamura@rmkb.com;anthony.arriola@rmkb.com
- David M Powlen david.powlen@btlaw.com, pgroff@btlaw.com
- Christopher E Prince cprince@lesnickprince.com, jmack@lesnickprince.com;cprince@ecf.courtdrive.com
- Lori L Purkey bareham@purkeyandassociates.com
- William M Rathbone wrathbone@grsm.com, jmydlandevans@grsm.com;sdurazo@grsm.com
- Jason M Reed Jason.Reed@Maslon.com
- Michael B Reynolds mreynolds@swlaw.com, kcollins@swlaw.com
- J. Alexandra Rhim arhim@hrhlaw.com
- Emily P Rich erich@unioncounsel.net, bankruptcycourtnotices@unioncounsel.net
- Robert A Rich , candonian@huntonak.com
- Lesley A Riis lriis@dpmclaw.com
- Debra Riley driley@allenmatkins.com
- Jason E Rios jrios@ffwplaw.com
- Julie H Rome-Banks julie@bindermalter.com
- Mary H Rose mrose@buchalter.com
- Megan A Rowe mrowe@dsrhealthlaw.com, lwestoby@dsrhealthlaw.com
- Nathan A Schultz nschultz@goodwinlaw.com
- Mark A Serlin ms@swllplaw.com, mor@swllplaw.com
- Seth B Shapiro seth.shapiro@usdoj.gov
- David B Shemano dshemano@shemanolaw.com
- Joseph Shickich jshickich@riddellwilliams.com
- Mark Shinderman mshinderman@milbank.com, dmuhrez@milbank.com;dlbatie@milbank.com
- Rosa A Shirley rshirley@nelsonhardiman.com, ksherry@nelsonhardiman.com;lgill@nelsonhardiman.com;rrange@nelsonhardiman.com
- Kyrsten Skogstad kskogstad@calnurses.org, rcraven@calnurses.org
- Michael St James ecf@stjames-law.com
- Andrew Still astill@swlaw.com, kcollins@swlaw.com
- Jason D Strabo jstrabo@mwe.com, cfuraha@mwe.com
- Sabrina L Streusand Streusand@slollp.com
- Ralph J Swanson ralph.swanson@berliner.com, sabina.hall@berliner.com
- Michael A Sweet msweet@foxrothschild.com, swillis@foxrothschild.com;pbasa@foxrothschild.com
- James Toma james.toma@doj.ca.gov, teresa.depaz@doj.ca.gov
- Gary F Torrell gtorrell@health-law.com
- United States Trustee (LA) ustpregion16.la.ecf@usdoj.gov
- Cecelia Valentine cecelia.valentine@nlrb.gov
- Jason Wallach jwallach@ghplaw.com, g33404@notify.cincompass.com

**NEF SERVICE LIST**

- Kenneth K Wang kenneth.wang@doj.ca.gov, Jennifer.Kim@doj.ca.gov;Stacy.McKellar@doj.ca.gov;yesenia.caro@doj.ca.gov
- Phillip K Wang phillip.wang@rimonlaw.com, david.kline@rimonlaw.com
- Sharon Z. Weiss sharon.weiss@bclplaw.com, raul.morales@bclplaw.com
- Adam G Wentland awentland@tocounsel.com, lkwon@tocounsel.com
- Latonia Williams lwilliams@goodwin.com, bankruptcy@goodwin.com
- Michael S Winsten mike@winsten.com
- Jeffrey C Wisler jwisler@connollygallagher.com, dperkins@connollygallagher.com
- Neal L Wolf nwolf@hansonbridgett.com, calendarclerk@hansonbridgett.com,lchappell@hansonbridgett.com
- Hatty K Yip hatty.yip@usdoj.gov, dare.law@usdoj.gov;kelly.l.morrison@usdoj.gov;kenneth.g.lau@usdoj.gov
- Andrew J Ziaja aziaja@leonardcarder.com, sgroff@leonardcarder.com;msimons@leonardcarder.com;lbadar@leonardcarder.com
- Rose Zimmerman rzimmerman@dalycity.org

94997640v.1

# EXHIBIT A

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

Attorneys for Defendant
UMB Bank, N.A. as master indenture trustee

**UNITED STATES BANKRUPTCY COURT**

**CENTRAL DISTRICT OF CALIFORNIA**

**LOS ANGELES DIVISION**

| | |
|---|---|
| In re<br><br>VERITY HEALTH SYSTEM OF CALIFORNIA, INC.<br><br>Debtors and Debtors in Possession.<br><br>OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., ET AL.,<br><br>Plaintiffs,<br><br>v.<br><br>UMB BANK, NATIONAL ASSOCIATION,<br><br>Defendant. | Case No.: 2:18-bk-20151-ER<br><br>Adv. No.: 2:19-ap-01166-ER<br><br>**NOTICE OF DEFENDANT'S MOTION AND MOTION TO DISMISS AMENDED COMPLAINT; MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT**<br><br>Hearing<br>Date: November 21, 2019<br>Time: 10:00 a.m.<br>Courtroom: 1568<br>Judge: Hon. Ernest M. Robles<br><br>Complaint Filed: June 13, 2019 |

**TO THE HONORABLE ERNEST M. ROBLES, UNITED STATES BANKRUPTCY COURT JUDGE, PLAINTIFF OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC. AND ITS COUNSEL OF RECORD, AND ANY OTHER PARTIES IN INTEREST:**

**PLEASE TAKE NOTICE THAT,** on November 21, 2019 at 10:00 a.m., or as soon thereafter as the matter may be heard before the Honorable Ernest M. Robles in Courtroom 1568 of the above-entitled Court, located at 255 E. Temple Street, Los Angeles, California, Defendant UMB Bank, National Association ("UMB" or "Defendant") will move (the "Motion") this Court for an order, pursuant to Federal Rules of Civil Procedure 12(b)(1) and 12(b)(6) (made applicable to this adversary proceeding by Federal Rule of Bankruptcy Procedure 7012), dismissing the *Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests*, dated June 13, 2019 [Adv. Docket No. 1] (the "Initial Complaint"), as amended by the *First Amended Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests*, [Adv. Docket. No. 28] (the "Amended Complaint"), filed by the Official Committee of Unsecured Creditors of Verity Health System of California, Inc., *et al.* (the "Committee" or "Plaintiff"), in its entirety for failure to state a claim upon which relief can be granted, or, in the alternative, dismissing Counts I and IV of the Complaint for lack of subject matter jurisdiction.

In support of this Motion, UMB relies on the filed pleadings, any documents or facts in the debtors' chapter 11 bankruptcy cases for which the Court may take judicial notice, the accompanying Memorandum of Points and Authorities in Support of Defendant's Motion to Dismiss the Amended Complaint, UMB's anticipated reply brief, applicable legal authority, and the arguments of counsel in support of this Motion.

**PLEASE TAKE FURTHER NOTICE** that, notwithstanding Local Bankruptcy Rule 9013-1, pursuant to the *Order Approving Stipulation Extending Time to Answer or Otherwise File Responsive Motion to Complaint*, dated August 30, 2019 [Adv. Docket No. 21], Plaintiff shall file any response to the Motion no later than October 17, 2019, and Defendant shall file any reply to Plaintiff's response no later than October 24, 2019.

DATED: September 30, 2019

Respectfully submitted,

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.

Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

-and-

Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

*Attorneys for UMB Bank, N.A. as master indenture trustee*

# PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is: 2029 Century Park East, Suite 3100, Los Angeles, CA 90067

A true and correct copy of the foregoing document entitled (*specify*): **NOTICE OF DEFENDANT'S MOTION AND MOTION TO DISMISS AMENDED COMPLAINT; MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT** will be served or was served **(a)** on the judge in chambers in the form and manner required by LBR 5005-2(d); and **(b)** in the manner stated below:

**1**. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**: Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On (*date*) September 30, 2019, I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

- Alexandra Achamallah aachamallah@milbank.com, rliubicic@milbank.com
- Nicholas A Koffroth nick.koffroth@dentons.com, chris.omeara@dentons.com
- Samuel R Maizel samuel.maizel@dentons.com, alicia.aguilar@dentons.com;docket.general.lit.LOS@dentons.com;tania.moyron@dentons.com;kathryn.howard@dentons.com;joan.mack@dentons.com;derry.kalve@dentons.com
- Tania M Moyron tania.moyron@dentons.com, chris.omeara@dentons.com;nick.koffroth@dentons.com
- Abigail V O'Brient avobrient@mintz.com, docketing@mintz.com;DEHashimoto@mintz.com;nleali@mintz.com;ABLevin@mintz.com;GJLeon@mintz.com
- Mark Shinderman mshinderman@milbank.com, dmuhrez@milbank.com;dlbatie@milbank.com
- United States Trustee (LA) ustpregion16.la.ecf@usdoj.gov

☐ Service information continued on attached page

**2. SERVED BY UNITED STATES MAIL**:
On (*date*) _____, I served the following persons and/or entities at the last known addresses in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

☐ Service information continued on attached page

**3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL** (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on (*date*) September 30, 2019, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

VIA FEDERAL EXPRESS
Honorable Ernest Robles
U.S. Bankruptcy Court
Roybal Federal Building
255 E. Temple Street, Suite 1560
Los Angeles, CA 90012

☐ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

| | | | |
|---|---|---|---|
| 9/30/19 | Diane Hashimoto | | /s/ Diane Hashimoto |
| *Date* | *Printed Name* | | *Signature* |

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

Attorneys for Defendant
UMB Bank, N.A. as master indenture trustee

**UNITED STATES BANKRUPTCY COURT**
**CENTRAL DISTRICT OF CALIFORNIA**
**LOS ANGELES DIVISION**

| | |
|---|---|
| In re<br><br>VERITY HEALTH SYSTEM OF CALIFORNIA, INC.<br><br>Debtors and Debtors in Possession.<br>OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., ET AL.,<br>Plaintiffs,<br>v.<br>UMB BANK, NATIONAL ASSOCIATION,<br>Defendant. | Case No.: 2:18-bk-20151-ER<br><br>Adv. No.: 2:19-ap-01166-ER<br><br>**MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT**<br><br>Hearing<br>Date: November 21, 2019<br>Time: 10:00 a.m.<br>Courtroom: 1568<br>Judge: Hon. Ernest M. Robles<br><br>Complaint Filed: June 13, 2019 |

**TABLE OF CONTENTS**

## TABLE OF AUTHORITIES[1]

**Page(s)**

**Cases**



[1] In accordance with Local Rule 9013-2(c)(3)(D), copies of any unpublished decisions cited herein are attached hereto as Exhibit 1.

**Other Authorities**

Defendant, UMB Bank, National Association, in its capacity as master indenture trustee ("UMB" or "Defendant"), files this memorandum of points and authorities in support of its motion (the "Motion to Dismiss") to dismiss the *Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests*, dated June 13, 2019 [Adv. Docket No. 1] (the "Initial Complaint"), as amended by the *First Amended Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests*, [Adv. Docket. No. 28] (the "Amended Complaint") filed by the Official Committee of Unsecured Creditors of Verity Health System of California, Inc., *et al.* (the "Committee" or "Plaintiff"), and respectfully states as follows:

**PRELIMINARY STATEMENT**

The Amended Complaint should be dismissed because it contains causes of action that have been directly rejected by the Ninth Circuit Court of Appeals and simply do not exist under law, have been asserted by Plaintiff for the first time after the deadline for bringing lien challenges has expired, are an attempt to re-write and collaterally attack the express, factual filings made by this Court more than one year ago in the Final DIP Order (as defined below) with respect to the valuation of UMB's collateral, and constitute an improper attempt to appeal the Final DIP Order long after any appeal period has run.

This adversary proceeding was brought as a "Lien Challenge" pursuant to ¶ 5(e) of the Final DIP Order. Pursuant to stipulations entered into between the parties, the deadline for bringing Lien Challenges expired on June 13, 2019 (the "Lien Challenge Deadline"). No further Lien Challenges may be brought. In the Initial Complaint, Plaintiff asserted only two substantive claims: (i) UMB does not have a valid lien on post-petition quality assurance fees ("QAF") (thus admitting the validity of UMB's lien on pre-petition QAF), and (ii) UMB did not have a valid prepetition lien on certain bank accounts (Plaintiff has stipulated that UMB did have a prepetition lien on six bank accounts that were subject to so-called "deposit account control agreements").

In its Amended Complaint, which was filed after the Lien Challenge Deadline, Plaintiff has added allegations in Count I which, for the first time, demand that this Court reduce or carve-out a so-called "going concern premium" from UMB's collateral, which would require this Court

to ignore its Petition Date valuation of Debtors' assets on a going concern sale basis as expressly set forth in the Final DIP Order. Instead, Plaintiff demands that this Court re-write its valuation on a liquidation or foreclosure sale basis, and give Plaintiff the difference between such liquidation value and the value achieved by Debtors' going concern sales, some of which have already closed and the remainder of which are scheduled to close shortly. Plaintiff's claim is nothing more than a conceptual bankruptcy policy argument that has been debated in academia. A long line of Ninth Circuit Court of Appeals precedent, along with well-established U.S. Supreme Court case law, makes clear that such a theory does not exist in the Ninth Circuit. In addition to the fact that this new claim is completely without support in law or in fact, it is also untimely because it requires the establishment of new and additional facts concerning valuation that were never raised in the Initial Complaint and, thus, do not "relate back" to the Initial Complaint.

Counts II and III of the Amended Complaint assert that UMB does not have a valid lien on certain of the Debtors' bank accounts (Count II) and on any of the Debtors' post-petition QAF payments (Count III). Counts II and III should be dismissed because they are moot. In its tentative ruling (which was incorporated into its final ruling), this Court expressly found and determined as an uncontroverted factual and evidentiary matter that the going concern sale value of the Debtors' assets subject to the secured liens in this case was $725 - $800 million, and that the total secured debt was $565 million, thereby resulting in an equity cushion of $150 – $225 million. As adequate protection for such equity cushion, and in consideration for the consent of the secured creditors to the priming liens required by the new DIP lender in an amount up to $186 million, the Final DIP Order granted an adequate protection lien to the secured creditors, including UMB. Such adequate protection lien is defined as the "Prepetition Replacement Lien" in ¶ 5(a) of the Final DIP Order. Given the priming nature of the new DIP Loan of up to $186 million, the Prepetition Replacement Lien is not just a so-called "rollover lien" in the same type of collateral that the secured creditors held prepetition; it is significantly broader, and encumbers virtually ***all*** assets of the Debtors.[2]

[2] The only assets excluded from the all-asset Prepetition Replacement Lien granted to UMB are Avoidance Actions (as defined in ¶ 5(e) of the Final DIP Order) and certain assets subject to the liens of specified

Thus, to the extent that UMB no longer enjoys the equity cushion found by this Court as of the Petition Date, UMB would be entitled to a judicially-granted Prepetition Replacement Lien pursuant to the Final DIP Order which would encumber all of the Debtors' remaining assets. The Plaintiff's claims that UMB may not have had a prepetition lien on certain bank accounts, or that UMB may not have a lien on post-petition QAF payments, is immaterial and moot based upon the terms and conditions of the Final DIP Order.

At the Final DIP Hearing (where Plaintiff was a full participant), Plaintiff never contested the Court's factual and evidentiary findings that UMB was oversecured and, otherwise, had an equity cushion and never contested that UMB was further entitled to the Prepetition Replacement Lien on all of the Debtors' assets that would protect UMB from any diminution in the value of such equity cushion. Plaintiff also never appealed those portions of the Final DIP Order. Plaintiff is now bound by such findings and should not be allowed to collaterally attack the Final DIP Order or, essentially, appeal its factual findings long after any appeal period has expired.

Plaintiff cannot have it both ways. It cannot rely upon this Court's factual findings from more than one year ago which justified the imposition of a priming lien on UMB's collateral and, otherwise, supported the DIP loans for its benefit, and now assert that the Court was wrong in making that valuation and that the adequate protection lien granted to UMB to protect against a diminution in UMB's equity cushion is no longer valid.

For the reasons stated in this Motion to Dismiss, UMB requests that the Amended Complaint be dismissed in its entirety with prejudice.

## FACTUAL AND PROCEDURAL BACKGROUND

### A. The Debtors Filed Bankruptcy for the Express Purpose of Selling Their Hospitals Pursuant to Going Concern Sales

On August 31, 2018 (the "Petition Date"), each of the Debtors in these jointly administrated cases filed a voluntary petition for relief under chapter 11 of title 11 of the United States Code (the

---

secured creditors as listed in ¶ 5(d) of the Final DIP Order, all of which are immaterial to the issues raised in this Motion to Dismiss.

"Bankruptcy Code"). As of the Petition Date, Verity Health System of California, Inc., a California nonprofit public benefit corporation, was the sole corporate member of, *inter alia*, the following acute care hospitals (collectively, the "Hospitals"): O'Connor Hospital ("O'Connor"); Saint Louise Regional Hospital ("St. Louise"); St. Francis Medical Center ("St. Francis"); St. Vincent Medical ("St. Vincent"); and Seton Medical Center and Seton Medical Center Coastside (collectively, "Seton"). *See Declaration of Richard G. Adcock in Support of Emergency First-Day Motions*, dated August 31, 2018 [Docket No. 8] (the "Adcock Declaration")[3] at ¶ 11.

The Debtors filed their bankruptcy cases for the express purpose of facilitating going concern sales (the "Sales") of all of the Debtors' highly leveraged Hospitals. *See id.* at ¶¶ 128-130; *Emergency Motion of Debtors for Interim and Final Orders (A) Authorizing The Debtors To Obtain Post Petition Financing (B) Authorizing The Debtors To Use Cash Collateral And (C) Granting Adequate Protection To Prepetition Secured Creditors Pursuant To 11 U.S.C. §§ 105, 363, 364, 1107 And 1108* [Docket No. 31] (the "Financing Motion") at ¶ 29. The Debtors did, in fact, sell each of their Hospitals as going concerns, which Sales have either closed or are scheduled to close shortly. St. Louise and O'Connor were sold for a gross purchase price of approximately $235 million subject to certain holdbacks and adjustments,[4] and St. Francis, St. Vincent and Seton are scheduled to be sold for a gross purchase price of $610 million before adjustments.[5] Together,

---

[3] Unless otherwise noted, all citations to "Docket No." are citations to the docket of the main bankruptcy proceeding, *In re Verity Health System of California, Inc. et al.*, Case No.: 2:18-bk-20151-ER.

[4] *See Debtors' Notice of Motion and Motion for the Entry of (I) an Order (1) Approving Form of Asset Purchase Agreement for Stalking Horse Bidder and for Prospective Overbidders; (2) Approving Auction Sale Format, Bidding Procedures and Stalking Horse Bid Protections; (3) Approving Form of Notice to be Provided to Interested Parties; (4) Scheduling a Court Hearing to Consider Approval of the Sale to the Highest Bidder; and (5) Approving Procedures Related to the Assumption of Certain Executory Contracts and Unexpired Leases; and (II) an Order (A) Authorizing the Sale of Property Free and Clear of All Claims, Liens, and Encumbrances; Memorandum of Points and Authorities in Support Thereof*, dated October 1, 2018 [Docket No. 365] at ¶ 32, as approved by Docket No. 1153.

[5] *See Debtors' Notice of Motion and Motion for the Entry of (I) an Order (1) Approving Form of Asset Purchase Agreement for Stalking Horse Bidder and for Prospective Overbidders; (2) Approving Auction Sale Format, Bidding Procedures and Stalking Horse Bid Protections; (3) Approving Form of Notice to be Provided to Interested Parties; (4) Scheduling a Court Hearing to Consider Approval of the Sale to the Highest Bidder; and (5) Approving Procedures Related to the Assumption of Certain Executory Contracts and Unexpired Leases; and (II) an Order (A) Authorizing the Sale of Property Free and Clear of All Claims,*

the Debtors' have sold their Hospitals for a gross purchase price in excess of $845 million (the "Sales Proceeds").[6]

**B. UMB's Secured Claims**

UMB serves as successor master trustee for the holders of nine series of debt securities which are owed a total of approximately $461 million, including the so-called 2005 Bonds, the 2015 Notes and the 2017 Notes. *See Declaration of Anita Chou, Chief Financial Officer, in Support of Motion for Interim Order Authorizing (A) Use of Cash Collateral; (B) Debtor in Possession Credit Agreement; (C) Grant of Superpriority Priming Liens to DIP Lender and: (D) Grant of Junior Liens on Postpetition Secured Parties Pursuant to 11 U.S.C. §§ 105(A), 363(C)(2), and 364(C) and (D)*, dated August 31, 2018 [Docket No. 32] at ¶ 3 - 4, as supplemented by a Supplemental Declaration [Docket No. 309-2] (collectively, the "Chou Declaration"). Wells Fargo Bank, National Association ("Wells Fargo"), serves as indenture trustee for the 2005 Bonds, having an outstanding principal balance of approximately $259 million. *Id*. U.S. Bank, National Association ("US Bank, and together with UMB and Wells Fargo, the "Prepetition Secured Creditors"), serves as indenture trustee for both the 2015 Notes and the 2017 Notes, which have an outstanding principal balance of approximately $202 million. *Id.*

The aggregate debt owed to the Prepetition Secured Creditors, $461 million, is secured by liens and security interests on most of the Debtors' primary assets (the "Prepetition Collateral"). In particular, UMB, as master trustee, has a lien on, among other things, (i) all real estate, property, plant and equipment of the Hospitals pursuant to duly recorded mortgages, and (ii) a lien on all personal property of the Hospitals pursuant to that certain Master Trust Indenture executed by each of the Hospitals as of December 1, 2001 (the "MTI"), including all revenues and intangibles of the Hospitals. This Court has recently ruled that the Hospitals' rights to QAF payments constitute

---

*Liens, and Encumbrances; Memorandum of Points and Authorities in Support Thereof,* dated January 17, 2019 [Docket No. 1279], Exhibit A (Asset Purchase Agreement) at 2, as approved by Docket No. 1572.

[6] In fact, the value of these Hospitals is greater than the gross combined $845 million Sales Proceeds, because in the case of the sale of St. Louise and O'Connor, the buyer did not purchase the hospitals' affiliated QAF or accounts receivable, which continue to be collected by the Debtors in the ordinary course.

license rights and, therefore, general intangibles under the Uniform Commercial Code.[7] Section 3.13 of the MTI provides, in pertinent part,

> Subject only to the provisions of this Master Indenture permitting the application thereof for the purposes and on the terms and conditions set forth herein, each Member, respectively, hereby pledges, and to the extent permitted by law grants a security interest to the Master Trustee in, the Gross Revenue Fund and all of the Gross Revenues of the Obligated Group to secure the payment of Required Payments and the performance by the Members of their other obligations under this Master Indenture.

In turn, "Gross Revenues" is defined in Section 1.01 of the MTI to mean, in relevant part,

> All revenues, income, receipts and money received by or on behalf of the Members from all sources, including (a) gross revenues derived from their operation and possession of each Member's facilities; . . . (c) proceeds derived from . . . (iv) inventory and other tangible and intangible property, (v) medical reimbursement programs and agreements, . . (vii) contract rights and other rights and assets now or hereafter owned by each Member . . . .

In addition to a lien on the Hospitals' prepetition QAF as "intangible property" (which lien has not been challenged by Plaintiff), UMB is also prepared, if necessary, to prove that every dollar contained in any bank account titled in the name of a particular Hospital is traceable to, and constitutes the proceeds of Gross Revenues of that Hospital, and is therefore subject to the security interests of UMB as described in the MTI.

UMB's liens are perfected by the recording of Deeds of Trust and by the filing of UCC-1 Financing Statements against each of the Hospitals. Once again, Plaintiff has not challenged the filing and perfection of any of UMB's liens.

Pursuant to that certain *Stipulation Between UMB Bank, N.A. and the Official Committee of Unsecured Creditors Extending Challenge Deadline,* entered December 13, 2018 [Docket No. 1049], Plaintiff has also acknowledged the validity of UMB's lien on certain bank accounts of the Hospitals (the "Acknowledged Bank Accounts") which are listed and described on Exhibit B to such stipulation.

---

[7] *See* Memorandum of Decision Authorizing Debtors to Sell Medi-Cal Provider Agreements, Free and Clear of Interests Asserted by the California Department of Health Care Services, Pursuant to § 363(F)(5), dated September 26, 2019 [Docket No. 3146] at 8.

Apart from its new claim for a "going concern premium," the Amended Complaint only challenges the scope of UMB's lien on post-petition QAF payments and on certain bank accounts other than the Acknowledged Bank Accounts.[8] Plaintiff has not challenged, and is now foreclosed from challenging, any other aspects of UMB's Prepetition Collateral.

**C. The Proceedings Relating To The Financing Motion Resulted In Uncontroverted Evidentiary Findings That UMB Holds An Equity Cushion, As Well As The Granting Of An Adequate Protection Lien On All Of The Debtors' Assets To Protect Against Any Diminution In Such Equity Cushion.**

Concurrently with the filing of these bankruptcy cases on the Petition Date, the Debtors filed their financing motion seeking to borrow up to $186 million from Ally Bank, secured by liens that would prime the security interests of UMB and the other Prepetition Secured Creditors. Amended Complaint at ¶ 16. The final hearing with respect to the Financing Motion was held on October 3, 2018 (the "Final DIP Hearing"). *See* Docket No. 392. At the Final DIP Hearing, the Court considered evidence submitted by the Debtors in the form of evidentiary declarations from a number of management level individuals employed by the Debtors and their professionals, including the Chou Declaration, the Adcock Declaration, and a Declaration submitted by James Maloney (the "Maloney Declaration"),[9] a Managing Director at the Debtors' investment bank, Cain Brothers (collectively, the "Declarations"). No party, including the Plaintiff, objected to the Declarations or the entry of the Declarations into evidence. No party, including the Plaintiff, introduced evidence that contradicted or rebutted any of the evidence and facts set forth in the Declarations.

---

[8] By the Amended Complaint, Plaintiff also seeks a finding that UMB does not have a security interest in assets related to medical office buildings (the "MOB Assets"). Amended Complaint at ¶ 25. This is an irrelevant allegation because UMB has never asserted a lien in the MOB Assets, and nothing in the Final DIP Order suggests otherwise.

[9] *Declaration Of James Maloney, In Support Of Motion For Final Order Authorizing (A) Use Of Cash Collateral; (B) Debtor In Possession Credit Agreement; (C) Grant Of Superpriority Priming Liens To DP Lender And; (D) Grant Of Junior Liens On Post Petition Accounts And Inventory As Adequate Protection To Prepetition Secured Parties Pursuant To 11 U.S.C. Sections 105(A), 363(C)(2), And 364(C) And (D),* dated September 26, 2018 [Docket No. 309-3].

In addition to detailing the amounts owed to the Prepetition Secured Creditors, the Declarations also presented evidence and facts relating to the value of the Prepetition Collateral. In summary, the Declarations stated that the aggregate secured debt was approximately $565 million, composed of $461 million owed to the Prepetition Secured Creditors, $40 million owed on account of so-called PACE financing, and $66 million owed to certain medical office building lenders; and that the approximate realizable value of the Debtors' assets exceeded the Debtors' secured debt by between $150 and $225 million. Thus, the uncontroverted evidence established that the Prepetition Secured Creditors had an equity cushion of between 26% and 40%. *See* Maloney Declaration at ¶ 9; Chou Declaration at ¶ 24.

At the Final DIP Hearing, based upon the evidentiary Declarations and the extensive oral argument presented by all of the parties, including the Plaintiff, the Court adopted its tentative ruling as the final ruling, dated October 3, 2018 [Docket No. 392] (the "Tentative Ruling"), and also made oral rulings and findings of fact with respect to the Financing Motion, including with respect to whether the value of the Prepetition Collateral exceeded the amount of the secured debt. The Tentative Ruling, which became final by virtue of incorporation into the Final DIP Order,[10] made the following findings of fact:

> II. Findings and Conclusions
>
> Based upon its review of the declarations of James Maloney and Anita Chou, the Court finds that the Debtor has submitted competent evidence establishing the need for the proposed financing from the DIP Lender. Specifically, as of the Petition Date, the book value of the Debtors' assets was approximately $857 million. Maloney Decl. [Doc. No. 309] at ¶8. After proper marketing, the aggregate realizable value of those same assets is in the range of $725 million to $800 million. *Id.* As of the Petition Date, aggregate secured claims against the Debtors totaled approximately $565 million. *Id.* at ¶9. The realizable value of the Debtors' assets, in excess of prepetition secured liabilities, is between $150–$225 million. *Id.*
>
> …
>
> The Court finds that the Secured Creditors whose liens are primed by the DIP Facility are adequately protected. The Maloney Decl. establishes that the aggregate

[10] *See Final DIP Order* at 6 (incorporating the Tentative Ruling by reference).

> secured debt on the Debtors' balance sheet as of the Petition Date was approximately $565 million. Maloney Decl. at ¶9. The approximate realizable value of the Debtors' assets, in excess of prepetition secured liabilities, is between $150 and $225 million. *Id.* **That is, secured creditors are protected by an equity cushion of between 26% to 40%.**

Tentative Ruling at 8 – 9 (emphasis added).

At no time prior to, or at the Final DIP Hearing did the Committee object, whether orally or in writing, to the factual findings that the Prepetition Secured Creditors had an equity cushion of at least $150 million. Moreover, the Committee failed to controvert or rebut any of the evidence presented by the Debtors, and did not introduce any of its own evidence with respect to valuation. In fact, the amount of Sales Proceeds realized (or to be realized upon closing) by the estates verifies and confirms the Court's finding at the beginning of these cases regarding the going concern value of the Debtors' assets.

The proposed DIP credit agreement stated that the consent of the Prepetition Secured Creditors to the Final DIP Order was a condition precedent to the DIP lender's obligation to commence making the revolving loans. *See* DIP Credit Agreement [Docket No. 32-4] at ¶ 3.3(b). This included consent to allow the liens securing the new DIP loan to prime the existing prepetition liens of the Prepetition Secured Creditors. At the Final DIP Hearing, the Prepetition Secured Creditors voluntarily agreed to allow such priming in return for the adequate protection contained in the Final DIP Order. "As adequate protection for the interests of the Prepetition Secured Creditors in the Prepetition Collateral …, on account of the granting of the [priming liens in favor of the DIP Lender], … the Prepetition Secured Creditors … shall receive adequate protection as follows: …". Final DIP Order at ¶ 5.

On October 4, 2018, the Bankruptcy Court entered the *Final Order (I) Authorizing Postpetition Financing, (II) Authorizing Use of Cash Collateral, (III) Granting Liens and Providing Superpriority Administrative Expense Status, (IV) Granting Adequate Protection, (V) Modifying Automatic Stay, and (VI) Granting Related Relief* [Docket No. 409] (the "Final DIP Order").

The adequate protection granted to the Prepetition Secured Creditors included "Prepetition Replacement Liens," which are defined in the Final DIP Order as "additional valid, perfected and enforceable replacement security interests and Liens in the DIP Collateral" to the extent of any diminution in value of the Prepetition Collateral. *See* Final DIP Order at ¶ 5(a). The "DIP Collateral" is comprised of "**all of the Debtors' property** ... whether arising before or after the Petition Date," subject to certain, limited exclusions which are inapplicable here. *Id.* at ¶ 2(d). In effect, the Prepetition Replacement Liens encumber virtually **all** of the Debtors' assets, and certainly include the Debtors' bank accounts and any post-petition QAF payments, both of which have been challenged by the Plaintiff and are the subject of the Amended Complaint.[11] The Tentative Ruling explained it succinctly:

> In addition to adequate protection through the equity cushion, the replacement liens and superpriority claims provide the secured creditors additional adequate protection. The financing provided by the DIP Lender will enable the Debtors to continue to operate and generate additional receivables. **Those receivables will be subject to the replacement liens**.

(emphasis added). Tentative Ruling at 9 – 10. Such "receivables" would certainly include any post-petition QAF payments.

At the Final DIP Hearing, the Committee was represented by counsel and its professionals, and lodged and presented numerous written and oral objections, none of which objected to the evidence submitted by the Debtors establishing the fact that UMB had an equity cushion, or that any language in ¶ 5(e) of the Final DIP Order contained a "mistake" (as alleged in Count I of the Amended Complaint). Further, Plaintiff did not object to the reaffirmation of such valuation evidence presented by Ms. Chou in her Declaration submitted in August 2019 in connection with

[11] Although the Final DIP Order uses the defined term "Prepetition Replacement Liens," it is a bit of a misnomer. The lien granted by the Final DIP Order does not merely "replace" the prepetition liens of the Prepetition Secured Creditors. It is a much broader security interest in all of the Debtors' assets to the extent of any diminution in the value of the Prepetition Collateral on and after the Petition Date, and is not akin to a so-called "rollover lien" that is typically limited to the types or categories of assets constituting Prepetition Collateral.

a supplemental motion to the Financing Motion. [12] Plaintiff did appeal the Final DIP Order (*see* Notice of Appeal [Docket No. 932]), but the subject of the appeal was extremely narrow, and was limited to objecting to the Section 506(c) waiver and the waiver of the "equities of the case" exception of Section 552(b).[13] The Committee did not appeal any other provision of the Tentative Ruling or the Final DIP Order.

**D. The Adversary Proceeding**

Pursuant to ¶ 5(e) of the Final DIP Order, the Committee had within ninety (90) days of its formation to challenge UMB's liens. As Plaintiff noted in the Initial Complaint, Plaintiff and UMB extended the Lien Challenge Deadline on several occasions, with the final extension expiring on June 13, 2019. *See* Initial Complaint ¶ 5. The Committee filed its Initial Complaint on the last possible day, and no further Lien Challenges could be brought after June 13th.

Pursuant to the *Stipulation Extending Time to Answer or Otherwise File Responsive Motion to Complaint,* [Adv. Docket No. 18], which was approved by the Court by order dated August 30, 2019 [Adv. Docket No. 21], Plaintiff was granted until September 11, 2019 to file an amended complaint, but UMB reserved all rights to answer or respond to such amended complaint on any grounds, including by contesting the timeliness of any new challenge, amended claim, or new cause of action. Plaintiff filed the Amended Complaint on September 11, 2019, well after the Lien Challenge Deadline.

The Counts in the Initial Complaint and in the Amended Complaint can be summarized as follows:

---

[12] *See Debtors' Notice of Motion and Motion for Entry of an Order (A) Authorizing the Debtors to Use Cash Collateral and (B) Granting Adequate Protection to Prepetition Secured Creditors; Memorandum of Points and Authorities; Declaration of Anita Chou in Support Thereof,* dated August 28, 2019 [Docket No. 2962] (the "Supplemental Cash Collateral Motion") at 39, ¶ 2.

[13] On August 2, 2019, the District Court dismissed the Committee's appeal. *See In re Verity Health Sys. Of Cal.*, Case No. 18-cv-10675-RGK, 2019 U.S. Dist. LEXIS 129797, at *15 (C.D. Cal. Aug. 2, 2019). The Committee has now further appealed to the Ninth Circuit Court of Appeals.

| Count | Allegations in the Initial Complaint | Allegations in the Amended Complaint |
|---|---|---|
| I | Final DIP Order must be amended because it contains a mistake | Final DIP Order must be amended because it contains a mistake<br><br>UMB does not have a lien in the "going concern premium" created in this case<br><br>UMB does not have a lien on the "MOB Assets" |
| II | UMB does not have a lien on certain prepetition bank accounts | UMB does not have a lien on certain prepetition bank accounts |
| III | UMB does not have a lien on post-petition QAF (no challenge to prepetition QAF) | UMB does not have a lien on post-petition QAF (no challenge to prepetition QAF)<br><br>UMB does not have a lien on post-petition QAF because, if any loan documents were amended to include post-petition QAF, such amendment is a fraudulent conveyance |
| IV | DOES NOT EXIST | If Plaintiff wins on any of Counts I – III, UMB is undersecured |

## ARGUMENT

### A. Count I Of The Amended Complaint Should Be Dismissed Pursuant To Rule 12(b)(6) Because Plaintiff's Argument That UMB Is Undersecured Due To The Existence Of A "Going Concern Premium" Is Not Cognizable As A Matter Of Law

#### 1. Legal Standard for Dismissal Pursuant to Rule 12(b)(6)

Under Federal Rule of Civil Procedure ("Rule")12(b)(6), made applicable to this proceeding by Federal Rule of Bankruptcy Procedure ("Bankruptcy Rule") 7012, this Court should dismiss any Counts of the Amended Complaint if they fail to state a claim upon which relief may be granted. "Dismissal may be based on either the lack of a cognizable theory or the absence of sufficient facts alleged under a cognizable legal theory." *Mangingdin v. Wash. Mut. Bank,* 637 F.Supp. 2d 700, 704 (N.D. Cal. 2009) (citing *Balistreri v. Pacifica Police Dep't,* 901 F.2d 696, 699 (9th Cir. 1990); *Robertson v. Dean Witter Reynolds, Inc.,* 749 F.2d 530, 534-34 (9th Cir.

1984). A complaint must give fair notice of the claim being asserted and the grounds upon which it rests. *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 570 (2007); *see also* Fed. R. Civ. P. 8(a)(2) (complaint must contain "a short and plain statement of the claim showing that the pleader is entitled to relief"). In addition to providing fair notice, the plaintiff must allege "enough facts to state a claim to relief." *Twombly*, 550 U.S. at 570. A claim is the "aggregate of operative facts which give rise to a right enforceable in the courts." *Bautista v. Los Angeles Cty.*, 216 F.3d 837, 840 (9th Cir. 2000); *see also Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (explaining that a claim is the set of "well-pleaded" factual allegations in a pleading which are intended by pleader to establish a "plausible" right to relief). When it is clear from the face of the complaint that a plaintiff has no entitlement to relief, it is appropriate for the Court to grant a motion to dismiss pursuant to Rule 12(b)(6). *See, e.g., Foley v. Wells Fargo Bank, N.A.*, 772 F.3d 63, 72 (1st Cir. 2014) "[A] primary purpose of a Rule 12(b)(6) motion is to weed out cases that do not warrant reaching the (oftentimes) laborious and expensive discovery process because, based on the factual scenario on which the case rests, the plaintiff could never win.").

Although the Court, in deciding whether the plaintiff has stated a claim, must take the plaintiff's allegations as true and draw all reasonable inferences in the plaintiff's favor, the court is not required to accept "merely conclusory" allegations, "unwarranted deductions of fact, or unreasonable inferences" as true. *See St. Clare v. Gilead Sciences, Inc.*, 536 F.3d 1049, 1055 (9th Cir. 2008); *see also Iqbal*, 556 U.S. at 678. "Pleadings must be something more than an ingenious academic exercise in the conceivable." *Jackson v. BellSouth Communs.*, 372 F.3d 1250, 1271 (11th Cir. 2004). In ruling on a motion to dismiss, the court may consider documents that are incorporated by reference but not physically attached to the complaint, if they are central to a plaintiff's claim and no party questions their authenticity. *See Marder v. Lopez*, 450 F.3d 445, 448 (9th Cir. 2006) (citations omitted).

**2. A Carve-Out From An Otherwise Valid Lien On Account Of A "Going Concern Premium" Is Merely A Theoretical, Conceptual Idea That Does Not Exist Outside Of Academia, Has No Support In The Bankruptcy Code Or Applicable Law, And Has Been Rejected Under Controlling Precedent In The Ninth Circuit.**

In Count I of the Amended Complaint, Plaintiff alleges, for the first time, that by continuing to operate the Debtors' business throughout the pendency of these cases, the Debtors generated a "going concern premium" that the Prepetition Secured Creditors would not have realized if the Prepetition Secured Creditors had theoretically foreclosed upon the Prepetition Collateral on the Petition Date. *See* Amended Complaint at ¶ 24. Plaintiff believes that its theory somehow requires this Court to reduce the value of UMB's security interest by the difference between such foreclosure value and the amount that the Debtors generated by disposing of UMB's collateral through the going concern sales. *Id.* This theory of law has been debated by academics on occasion in the past and continues, from time to time, to be the subject of a handful of law review articles analyzing whether bankruptcy law policy should be radically changed. *See, e.g.*, David G. Baird, *The Rights of Secured Creditors after* ResCap, 2015 University of Illinois Law Review 849 (2015) (arguing that the theory is unsupportable and, in any event, is directly contrary to existing law).

There is no debate in the Ninth Circuit. Controlling precedent from the Ninth Circuit Court of Appeals, which was decided within the last two years, is clear that a secured creditor's collateral must be valued based upon the intended use or disposition of such collateral, not solely upon a liquation basis. *First Southern Nat'l Bank v. Sunnyslope Hous. L.P. (In re Sunnyslope Hous. L.P.*) 859 F.3d 637 (9th Cir. 2017). In *Sunnyslope*, the Ninth Circuit Court of Appeals held:

> We established long ago that, '[w]hen a Chapter 11 debtor or a Chapter 13 debtor intends to retain property subject to a lien, the purpose of a valuation under section 506(a) is not to determine the amount the creditor would receive if it hypothetically had to foreclose and sell the collateral.' The debtor is 'in, not outside of, bankruptcy,' so '[t]he foreclosure value is not relevant' because the creditor 'is not foreclosing.'

859 F.3d 637, 644 (9th Cir. 2017) (en banc) (quoting *In re Taffi,* 96 F.3d 1190, 1192 (9th Cir. 1996) (en banc), *cert. denied,* 138 L. Ed. 2d 987, 117 S. Ct. 2478 (1997)).

*Sunnyslope* (and *Taffi*) are only two of the long-standing, consistent precedents in the Ninth Circuit which reject the lynchpin of Plaintiff's theory. In *Salyer v. SK Foods, L.P. (In re SK Foods, L.P.),* 487 B.R. 257, 262 (E.D. Cal. 2013), the court affirmed the bankruptcy court's approval of a compromise reached between a trustee and a secured lender regarding the amount of the lender's deficiency superpriority claim, finding that the bankruptcy court properly valued the debtors' assets "in connection with the Debtors' use of the creditors' cash collateral, enabling the debtor to keep running the business, and in contemplation of the going concern sale." The court rejected any argument that the bankruptcy court should have used liquidation value in determining the amount of the lender's secured claim, because a going concern sale was always contemplated, and in fact was what happened. *Id. See also In re Kim,* 130 F.3d 863, 865 (9th Cir. 1997) (finding that value of entire dry cleaning business, which included the goodwill generated by continuing to operate the business in the same location, should be included in valuing the secured creditors' collateral); *see also Bond v. Kerns*, Case No. CV-12-00875-TUC-RCC, 2013 U.S. Dist. LEXIS 184286, *5-6 (D. Ariz. Dec. 16, 2013) (collecting cases) ("A number of cases, both from this circuit and others, come to essentially the same conclusion: when a debtor plans to continue operation of a business, the business should be valued as a going concern."); *In re Hawaiian Telcom Communs., Inc.*, 430 B.R. 564, 604 (Bankr. D. Hi. 2009) (citing cases) ("Where debtors intend to reorganize and continue to operate their business, and prospects for reorganization appear favorable, collateral should be valued using the going concern value for purposes of determining the extent of the creditor's secured claim under section 506(a).")

The entire premise of Plaintiff's purely academic concept, *i.e.*, that the value of a secured creditor's collateral should be measured on the petition date only at liquidation value, is not only directly contrary to controlling Ninth Circuit precedent, but is also directly contrary to well-known U.S. Supreme Court precedent. Like the Ninth Circuit Court of Appeals in *Sunnyslope,* the Supreme Court has been very clear, dating back to 1997, that the method of valuation of a secured

creditor's collateral is dependent upon the intended use or disposition of such collateral. *Assocs. Commer. Corp. v. Rash*, 520 U.S. 953, 962 (1997). In *Rash*, the Supreme Court stated, "[a]s we comprehend § 506(a), the 'proposed disposition or use' of the collateral is of paramount importance to the valuation question."). *Id*. Plaintiff's claim that this Court should carve-out a "going concern premium" from UMB's collateral is simply not cognizable in the Ninth Circuit as a matter of law.

The Debtors' stated purpose of these bankruptcy cases has never wavered: they have sought to maintain the going concern value of the Hospitals and related assets so as to pursue going-concern sales. *See, e.g.*, Adcock Declaration at ¶ 128-130; Financing Motion at ¶ 29. It was always intended that the Prepetition Collateral would be sold as a going concern and not pursuant to a liquidation. The Amended Complaint itself cites to the fact that the Court has entered orders approving the sale of O'Connor and St. Louise, which sale has closed, and the Court has approved the sale of St. Francis, St. Vincent and Seton, which is expected to close shortly. Amended Complaint at ¶ 22. Under *Sunnyslope* and its predecessors, the value of UMB's lien as of the Petition Date is measured by reference to the Prepetition Collateral's going concern sale value, not by reference to some theoretical foreclosure value. As noted by the Ninth Circuit in *Sunnyslope*, foreclosure value is simply not relevant because the secured creditor (in this case, UMB) did not foreclose. *Sunnyslope*, 859 F.3d at 644. This valuation methodology is, in fact, what the Court utilized, was never contested by the Plaintiffs, and its choice of valuation methodologies has been proven to be entirely correct through the approved sales during these proceedings.

To the extent that Count I includes this discredited theory, it should be dismissed pursuant to Rule 12(b)(6) with prejudice for failure to state a claim upon which relief can be granted.

**B. Plaintiff's So-Called "Going Concern Premium" Theory Can Also Be Dismissed As Untimely, Because The Deadline For Bringing Lien Challenges Has Expired And Such Claim Does Not Relate Back To The Causes Of Action In The Initial Complaint.**

Plaintiff's "going concern premium" theory is a new Lien Challenge which does not appear in the Initial Complaint in any form, and only surfaced for the first time in the Amended Complaint, well beyond the Lien Challenge Deadline. *See* Amended Complaint ¶¶ 22-25. The Initial Complaint was limited to alleging that UMB did not have a lien on certain bank accounts and post-petition QAF payments. Now, in the Amended Complaint, Plaintiff added its new theory that UMB also did not have a lien on the so-called "going concern premium" of the Debtors. In addition to adding its new claim in the Amended Complaint, Plaintiff also added new facts that, once again, did not appear in the Initial Complaint but, according to Plaintiff, are necessary to support its new "going concern premium" theory. *Id.*

Plaintiff was only entitled to amend the Initial Complaint after the expiration of the Challenge Deadline (*viz.*, June 13, 2019), if its new claims and supporting evidence qualify under the "relation-back" doctrine. Since Plaintiff's new theory and, in particular, its new supporting facts, did not appear in, and are unrelated to the claims in the Initial Complaint, the new claim does not relate-back to the Initial Complaint. Plaintiff's new "going concern premium" theory is time-barred and should be dismissed with prejudice.

**1. "Relation-Back" Standard Under Rule 15**

Pursuant to Rule 15, made applicable to this proceeding by Bankruptcy Rule 7015, a claim which is otherwise time-barred may survive to the extent that it "relates back" to a timely-filed pleading under certain circumstances, namely, if "the claim or defense asserted in the amended pleading arose out of the conduct, transaction or occurrence set forth or attempted to be set forth in the original pleading…" *See* Fed. R. Civ. P. 15(c)(2). Under Ninth Circuit case law, such a link will only be found "when 'the claim to be added will likely be proved by the same kind of evidence offered in support of the original pleading.'" *See Magno v. Rigsby (In re Magno)*, 216 B.R. 34, 39 (B.A.P. 9th 1997) (quoting *In re Dominguez*, 51 F.3d 1502, 1508 n. 5 (9th Cir. 1995)). "[A]n amendment can only relate back if the new claim relies on the same facts and does not seek to insert new facts." *Id.* at 41 (citations omitted) (reversing bankruptcy court's order granting leave to amend because untimely amended complaint pleaded new theory as well as new facts).

In a recently decided case, *Echlin v. PeaceHealth*, the Ninth Circuit articulated the controlling standard as follows:

> [C]laims must share a common core of operative facts such that the plaintiff will rely on the same evidence to prove each claim. Thus, an amendment will not relate back when the amended complaint had to include additional facts to support the new claim.

887 F.3d 967, 978 (9th Cir. 2018) (internal citations omitted). *Echlin* determined that, although the added claim arose from the same general transaction, the original complaint failed to allege at least two facts critical to support the added claim. *Id.* Accordingly, the new claims would not relate back, and were therefore untimely. *Id.* at 979.

Likewise, in *Williams v. Boeing Co.*, 517 F.3d 1120, 1133 (9th Cir. 2008), the Ninth Circuit Court of Appeals found that there was no common core of operative facts between the newly asserted claim and the claims asserted in the original pleadings because the second amended complaint had to include additional facts in order to prove the new claims. The new claim did not "relate back" because

> different statistical evidence and witnesses would be used to prove the [new] compensation and [earlier] promotion discrimination claims because of the different processes ... used to make salary and promotion decisions ... The compensation discrimination claim is a new legal theory depending on different facts, not a new legal theory depending on the same facts.

*Id.*

In order to save a time-barred claim from dismissal pursuant to Rule 15, its viability must not be dependent upon the assertion of new facts that a plaintiff failed to assert in the previously timely filed pleading.

**2. The Newly-Added "Going Concern Premium" Cause Of Action Is Based On Alleged Facts Not Included In The Initial Complaint; As Such, It Does Not Relate-Back To The Initial Complaint And, Since the Challenge Deadline Has Expired, It Must Be Dismissed Without Leave To Amend.**

Plaintiff's contention that any "going concern premium" generated by the estates should be excluded from UMB's Prepetition Collateral requires the assertion of new facts not contained in the Initial Complaint. The blackline version of the Amended Complaint [Docket No. 28-1]

shows that, in order to attempt to support its new claim, Plaintiff alleged new facts in ¶¶ 22-24. In addition, in order to try to support its new claim, Plaintiff will need to establish evidence that was never implicated nor would have been required under the Initial Complaint, *e.g.*, the foreclosure value of the Prepetition Collateral as of the Petition Date, the amount of attendant wind-down costs, and the value of the labor which Plaintiff asserts is responsible for any going concern premium. *Id.* None of these issues were in any way raised in the Initial Complaint, which was limited to challenging UMB's lien on prepetition bank accounts and post-petition QAF payments. Much like in *Williams*, this new claim does not come from a common core of operative facts; rather entirely, different evidence and witnesses will be required to prove this new legal theory. Even though, like in *Echlin*, the new claim may be viewed as having arisen from the same general transaction, Plaintiff failed to allege sufficient facts to support this new claim before the Lien Challenge Deadline, and, accordingly, it does not relate back to the Initial Complaint and is time barred.

**C. Counts II And III Of The Amended Complaint Are Moot Because This Court Has Found That UMB Has An Equity Cushion And Has Been Granted An Adequate Protection Lien On Virtually All Of The Debtors' Post-Petition Assets In The Event That There Is Any Diminution In The Value Of Such Equity Cushion.**

This Court has already expressly found and determined that, as of the Petition Date, the Prepetition Secured Creditors' aggregate secured debt was approximately $565 million; the aggregate realizable value of the collateral securing that debt was in the range of $725 million to $800 million; and, therefore, the aggregate value of the Prepetition Collateral exceeds the secured debt in this case by approximately 26 – 40%. Tentative Ruling at 8-9 (incorporated by reference in the Final DIP Order at 6).

The Final DIP Order was hotly contested and carefully worded to provide adequate protection to the Prepetition Secured Creditors, especially in light of the fact that it provided for the DIP lender to prime the otherwise first priority prepetition liens of the Prepetition Secured Creditors up to the maximum amount of $186 million. One of the central aspects of such adequate protection is ¶ 5(e), which provides that, if there is any overall diminution in the value of UMB's

Prepetition Collateral, UMB will be entitled to a "Prepetition Replacement Lien" (as defined in the Final DIP Order). Per the explicit definition in the Final DIP Order, if UMB's equity cushion diminishes in value, the Prepetition Replacement Lien would encumber **all** of the Debtors' assets to the extent of such diminution. In other words, even if Plaintiff's allegations in the Amended Complaint are correct, to the extent that UMB suffers a diminution in value of its overall prepetition collateral, it will be entitled to a lien on all of the Debtors' post-petition assets. Any other conclusion would effectively ignore and indirectly reverse this Court's evidentiary findings regarding the value of UMB's debt, the value of the Prepetition Collateral, and the finding that the Prepetition Secured Creditors have a 26 – 40% equity cushion. Those findings were necessary predicates for the Court to rule that UMB's prepetition liens were adequately protected and could be subordinated to, and primed by, $186 million in liens granted to the DIP lender under the Final DIP Order.

Plaintiff was a full participant at the hearing on the Final DIP Order but failed to object to the Court's factual findings regarding UMB's equity cushion; failed to present any rebuttal evidence to the Debtors' evidence of value; and failed to object to the application or scope of the Prepetition Replacement Lien as defined in the Final DIP Order. Pursuant to Rule 9013-1(i)(2) of the Local Bankruptcy Rules of the United States Bankruptcy Court for the Central District of California, the Plaintiff thereby waived any evidentiary objections to such factual findings. After the Final DIP Order was entered, Plaintiff also failed to appeal the valuation findings made by the Court. Plaintiff is now bound by such findings and cannot indirectly attack the Court's overall valuation finding by attempting to contest the prepetition value of an individual item of UMB's Prepetition Collateral. *See, e.g., Wiersma v. Bank of the West (In re Wiersma),* 483 F.3d 933, 941 (9th Cir. 2006) (quoting *Hydrick v. Hunter,* 466 F.3d 676, 687 (9th Cir. 2006) (quoting *Richardson v. United States,* 841 F.2d 993, 996 (9th Cir. 1988)))("Under the 'law of the case' doctrine, a court is ordinarily precluded from reexamining an issue previously decided by the same court, or a higher court, in the same case.").

Plaintiff has also expressly admitted that an equity cushion exists, and it should not be allowed to take the contrary position merely when to do so is convenient. Plaintiff's inconsistent positions are highlighted, for example, by the arguments made in its current appeal of the Final DIP Order.[14] Plaintiff directly relied upon this Court's determination that the Prepetition Secured Creditors have an equity cushion, and then unsuccessfully attempted to use that factual finding to argue that the Prepetition Secured Creditors were not entitled to any waivers in the Final DIP Order. *See* Appellate Brief at 19 (questioning why the Section 502(c) and 552(b) waivers were necessary to the Prepetition Secured Creditors, "whom the Bankruptcy Court had found were already fully protected by an equity cushion in excess of 25%").

The express terms of the DIP credit agreement stated that it was a condition precedent that none of the Prepetition Secured Creditors opposed the Final DIP Order.[15] It would be unjust to let Plaintiff have it both ways – allow Plaintiff to argue that the Court made a mistake in valuing UMB's Prepetition Collateral, but at the same time receive the benefit of the postpetition loans. The inequity is especially pronounced at this late date, well after tens of millions of dollars of DIP loans have already been lent, which primed UMB's prepetition liens, and UMB consented to the use of the proceeds of the sale of O'Connor and St. Louise to allow the Debtors to repay the DIP loans.[16]

In short, regardless whether Plaintiff prevails, the Final DIP Order is clear that, if UMB's claim is not satisfied by virtue of the proceeds of its prepetition security interests because of a diminution in such collateral, thereby triggering the Prepetition Replacement Lien, UMB will be entitled to a lien on all of the Debtors' remaining assets. The relief requested by Counts II and III

---

[14] *See Appellant Official Committee of Unsecured Creditors' Appellant's Brief,* District Court Case No. 2:188-cv-10675-RGK, dated March 14, 2019 [Docket No. 22] ("Appellant's Brief") at 2, 17-19.

[15] DIP Credit Agreement [Docket No. 32-4] at ¶ 3.3(b).

[16] *See Final Order (A) Authorizing Continued Use of Cash Collateral, (B) Granting Adequate Protection, (C) Modifying Automatic Stay, and (D) Granting Related Relief,* dated September 6, 2019 [Docket No. 3022] (the "Supplemental Cash Collateral Order") at ¶ H(ii).

of the Amended Complaint is moot. This Court should dismiss Counts II and III of the Amended Complaint in their entirety, without leave to amend.[17]

**D. Count II Should Be Dismissed As Moot Because All Of The Money In The Relevant Bank Accounts Has Long Since Been Used And Spent By The Debtors, And There Is No Cash Remaining To Be Recovered By Plaintiff.**

In Count II of the Amended Complaint, Plaintiff claims that UMB did not have a valid prepetition lien in the cash in certain bank accounts other than the Acknowledged Bank Accounts. As of the Petition Date, the Debtors' cash on hand was less than $40 million. Chou Declaration ¶ 12. On average, the Debtors have experienced losses of approximately $450,000 per day.[18] Given the limited cash on hand on the Petition Date, and the substantial ongoing losses which the Debtors have incurred since the beginning of this case, it is beyond question that any cash in any bank accounts existing as of the Petition Date has long since been withdrawn and spent by the Debtors during the course of these cases. In fact, in addition to completely exhausting the cash which existed in their bank accounts as of the Petition Date, the Debtors have burned through more than $100 million in draws under the Ally Bank DIP facility, and are now drawing and spending the cash collateral of the Prepetition Secured Creditors which arose from the sale of O'Connor and St. Louise. *See Supplemental Cash Collateral Order* at ¶ H. Even if Plaintiff prevails on Count II, there is no cash existing as of the Petition Date which remains in any bank account to be recovered by Plaintiff. The money is gone. Count II should be dismissed because it is moot and fails to present a real case or controversy for which relief can be granted.

**E. Counts I And Count IV Of The Amended Complaint Should Be Dismissed Because They Are A Disguised Attempt To Appeal The Final DIP Order Long After The Time For An Appeal Has Expired.**

In addition to the "going concern premium" claim, Count I of the Amended Complaint seeks a declaratory judgment asking the Court to modify and amend the words and language of ¶

[17] The Amended Complaint contains an amendment to Count III pursuant to which Plaintiff asserts a constructive fraudulent conveyance claim "to the extent Defendant contends one or more Loan Agreements were modified to include a lien in Future QAF Disbursements…" *See* Amended Complaint at ¶ 36. For the avoidance of doubt, for purposes of this Motion to Dismiss, Defendant makes no such contention.

[18] *See* Supplemental Cash Collateral Motion at ¶ 15.

5(e) of the Final DIP Order, which was entered on October 4, 2018, almost one year ago. Count IV of the Amended Complaint, which is a newly added Count, seeks a declaratory judgment that, if Plaintiff prevails on any of the other Counts, UMB is "undersecured." The Court should dismiss both Count I and Count IV pursuant to Rule 12(b)(1) for lack of subject matter jurisdiction because Plaintiff's claims are simply disguised attempts to circumvent the jurisdictional bar to pursue an appeal after the expiration of the appeal period.

Federal courts are courts of limited jurisdiction. *See Kokkonen v. Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 377 (1994). The burden of establishing that the court has jurisdiction over a claim rests with the party asserting jurisdiction. *Id.* Lack of subject matter jurisdiction may be raised at any point during the litigation through a motion to dismiss pursuant to Rule 12(b)(1). *See Int'l Union of Operating Eng'rs v. Cnty. Of Plumas,* 559 F.3d 1041, 1043 (9th Cir. 2009). The failure to timely appeal is a jurisdictional defect. *See, e.g., Wiersma,* 483 F.3d at 938 (quoting *Lopez v. Long (In re Long),* 255 B.R. 241, 243 (B.A.P. 10th Cir. 2000)) ("The failure to timely file a notice of appeal is a jurisdictional defect barring appellate review."); *See also Taylor v. L.A. County Tax Collector,* CV 13-09316 BRO (PLAx), 2014 U.S. Dist. LEXIS 195759, at*6-7 (C.D. Cal. Feb. 7, 2014) (dismissing action with prejudice for lack of subject matter jurisdiction, as plaintiff failed to appeal order within time limits ascribed by Bankruptcy Rule 8002).

Count I seeks a declaratory judgment to interpret the language of ¶ 5(e) of the Final DIP Order because, according to the Committee, it "mistakenly suggests that Defendant has a security interest in all of the assets of all of the Debtors." Amended Complaint at ¶ 30. Additionally, Count IV seeks a declaratory judgment that, if Plaintiff prevails on any of its other claims, UMB is undersecured. *See id.* at ¶ 39. In effect, the Committee wants to amend and modify the language of ¶ 5(e) of the Final DIP Order, as well as challenge the Court's evidentiary finding that UMB holds an equity cushion as of the Petition Date. Such requests are tantamount to raising an objection to the terms of the Final DIP Order almost a year after it was entered. The Committee failed to raise any such objection to ¶ 5(e), either in its written objection [Docket No. 316] before the Final DIP Hearing or at the Final DIP Hearing. The Committee certainly considered an appeal

of the Final DIP Order because it did, in fact, appeal, but that appeal was limited solely to the 506(c) waiver and the waiver of the "equities of the case" exception of Section 552(b), and did not even mention ¶ 5(e) or any alleged "mistake." The Committee should not now be allowed to circumvent the requirement to bring timely objections at or before the Final DIP Hearing, or the requirement to appeal orders within the 14-day appeal period prescribed by Bankruptcy Rule 8002. Nor should Plaintiff be allowed to circumvent this jurisdictional hurdle by an assertion of "mistake" in the heavily negotiated Final DIP Order, particularly when it could have, but failed, to seek timely relief under Rule 60(b)(1). Counts I and IV should be dismissed with prejudice as untimely.

## CONCLUSION

For the reasons stated above, each of the Counts of the Amended Complaint should be dismissed, with prejudice.

DATED: September 30, 2019

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.

Daniel S. Bleck (*pro hac vice*)
Paul J. Ricotta (*pro hac vice*)
Ian A. Hammel (*pro hac vice*)
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

-and-

Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

*Attorneys for UMB Bank, N.A. as master indenture trustee*

# EXHIBIT 1

Neutral
As of: September 30, 2019 8:45 PM Z

# *In re Verity Health Sys. of California, Inc.*

United States Bankruptcy Court for the Central District of California, Los Angeles Division

August 2, 2019, Decided; August 2, 2019, Filed & Entered

Lead Case No. 2:18-bk-20151-ER, Jointly Administered with: Case No. 2:18-bk-20162-ER, Case No. 2:18-bk-20163-ER, Case No. 2:18-bk-20164-ER, Case No. 2:18-bk-20165-ER, Case No. 2:18-bk-20167-ER, Case No. 2:18-bk-20168-ER, Case No. 2:18-bk-20169-ER, Case No. 2:18-bk-20171-ER, Case No. 2:18-bk-20172-ER, Case No. 2:18-bk-20173-ER, Case No. 2:18-bk-20175-ER, Case No. 2:18-bk-20176-ER, Case No. 2:18-bk-20178-ER, Case No. 2:18-bk-20179-ER, Case No. 2:18-bk-20180-ER, Case No. 2:18-bk-20181-ER, Chapter 11 Cases

**Reporter**
2019 Bankr. LEXIS 2470 *; 2019 WL 3577535

In re VERITY HEALTH SYSTEM OF CALIFORNIA, INC., et al., Debtors and Debtors In Possession. Affects Verity Health System of California, Inc., Affects St. Francis Medical Center, Debtors and Debtors In Possession.

## Core Terms

automatic stay

**Counsel: [*1]** For Verity Health System of California, Inc., Debtor (2:***18-bk-20151-ER***): Sam J Alberts, DENTONS US LLP, Washington, DC; Shirley Cho, Pachulski Stang Ziehl & Jones LLP, Los Angeles, CA; Steven J Kahn, Los Angeles, CA; Patrick Maxcy, Dentons US LLP, Chicago, IL; Claude D Montgomery, Dentons US LLP, New York, NY; Nicholas A Koffroth, Samuel R Maizel, John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:***18-bk-20151-ER***): Alvin Mar, Los Angeles, CA; Hatty K Yip, Office of the UST, Los Angeles, CA.

For Official Committee of Unsecured Creditors of Verity Health System of California, Inc., et al., Creditor Committee (2:***18-bk-20151-ER***): Alexandra Achamallah, James Cornell Behrens, Milbank LLP, Los Angeles, CA; Robert M Hirsh, Arent Fox LLP, New York, NY.

For St. Louise Regional Hospital, Debtor (2:18-bk-20162-ER): John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20162-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For Verity Business Services, Debtor (2:18-bk-20173-ER): Samuel R Maizel, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), **[*2]** U.S. Trustee (2:18-bk-20173-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For St. Francis Medical Center of Lynwood Foundation, Debtor (2:18-bk-20178-ER): Samuel R Maizel, John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20178-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For De Paul Ventures, LLC, Debtor (2:18-bk-20176-ER): Samuel R Maizel, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20176-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For O'Connor Hospital Foundation, Debtor (2:18-bk-20179-ER): Samuel R Maizel, John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20179-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For St. Vincent Foundation, Debtor (2:18-bk-20180-ER): Samuel R Maizel, John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20180-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For De Paul Ventures - San Jose Dialysis, LLC, Debtor (2:18-bk-20181-ER): Samuel R Maizel, Tania M Moyron, Dentons **[*3]** US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20181-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For Verity Holdings, LLC, Debtor (2:18-bk-20163-ER): Samuel R Maizel, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee: Hatty K Yip, Office of the UST/, Los Angeles, CA.

For St. Vincent Medical Center, Debtor (2:18-bk-20164-ER): Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20164-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For St. Francis Medical Center, Debtor (2:18-bk-20165-ER): John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20165-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For Seton Medical Center, Debtor (2:18-bk-20167-ER): John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20167-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For O'Connor Hospital, Debtor (2:18-bk-20168-ER): John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20168-ER): **[*4]** Hatty K Yip, Office of the UST, Los Angeles, CA.

For Verity Medical Foundation, Debtor (2:18-bk-20169-ER): Crystal Johnson, AT and T, Fort Worth, TX; Samuel R Maizel, John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20169-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For St. Vincent Dialysis Center, Inc., Debtor (2:18-bk-20171-ER): John A Moe, II, Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20171-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

For Saint Louise Regional Hospital Foundation, Debtor (2:18-bk-20172-ER): Tania M Moyron, Dentons US LLP, Los Angeles, CA.

For United States Trustee (LA), U.S. Trustee (2:18-bk-20172-ER): Hatty K Yip, Office of the UST, Los Angeles, CA.

**Judges:** Hon. Ernest M. Robles, United States Bankruptcy Judge.

**Opinion by:** Ernest M. Robles

## Opinion

**ORDER GRANTING MOTION FOR RELIEF FROM THE AUTOMATIC STAY ON BEHALF OF FEDERICO FUENTES, AND IRENE FUENTES [DOCKET NO. 2504]**

*The Motion For Relief From The Automatic Stay* (the "Motion") [Docket No. 2504], filed on behalf of Federico Fuentes and Irene Fuentes, was scheduled for hearing at 10:00 a.m. on Monday, **[*5]** July 29, 2019, in Courtroom 1568, Roybal Federal Building, 255 East Temple Street, Los Angeles, California 90012. The parties rested on the Court's Tentative Ruling issued July 26, 2019, which (1) approved the parties' *Stipulation Between Debtors Verity Health System Of California, Inc., St. Francis Medical Center And Federico Fuentes And Irene Fuentes Granting Motion For Relief From The Automatic Stay* [Docket No. 2722] (the "Stipulation"), (2) vacated the hearing and (3) requested that the Debtors' counsel lodge an Order.

Upon consideration of the Motion and the Stipulation, it appearing that proper notice of the Motion and Stipulation had been provided, and for the reasons set forth in the Court's Tentative Ruling on the Motion, and good and sufficient cause having been shown,

IT IS HEREBY ORDERED that:

1. The Motion is granted.
2. Pursuant to the terms of the Stipulation:

a. Relief from the automatic stay shall not be effective until August 15, 2019.

b. Federico Fuentes and Irene Fuentes shall seek recovery only from applicable insurance and waive any deficiency or other claim against the Debtors or property of the Debtors' bankruptcy estate.

c. Federico Fuentes and Irene Fuentes will **[*6]** not assert causes of action against the Debtors that are

not covered by insurance.

Date: August 2, 2019

/s/ Ernest M. Robles

Ernest M. Robles

United States Bankruptcy Judge

---

**End of Document**

# Bond v. Kerns

United States District Court for the District of Arizona

December 13, 2013, Decided; December 16, 2013, Filed

No. CV-12-00875-TUC-RCC

**Reporter**
2013 U.S. Dist. LEXIS 184286 *; 2013 WL 7046375

Mark Bond and Ashlea Bond, Appellants, v. Dianne C. Kerns, et al., Appellees.

**Prior History:** *In re Bond, 2012 Bankr. LEXIS 4107 (Bankr. D. Ariz., Sept. 5, 2012)*

## Core Terms

valuation, liquidation value, cases, bankruptcy court, calculate

**Counsel:** **[*1]** For Mark Bond, Debtors, Ashlea Bond, Debtors, Appellants: H Lee Horner, Jr., LEAD ATTORNEY, Goldstein Horner & Horner Attorneys, Cortaro, AZ.

Dianne C Kerns, Chapter 13, Trustee, Appellee, Pro se, Tucson, AZ.

For Prince Road Associated LLC, Appellee: Karl E MacOmber, LEAD ATTORNEY, Monroe & McDonough PC, Tucson, AZ.

**Judges:** Raner C. Collins, Chief United States District Judge.

**Opinion by:** Raner C. Collins

## Opinion

**ORDER**

Pending before the Court is Appellants' appeal from the Bankruptcy Court's dismissal of their Chapter 13 case. This matter has been fully briefed, and the Court heard oral arguments on December 12, 2013. For the following reasons, the Court will dismiss the appeal.

**I. Background**

The Bonds have a 70% interest in AMG Enterprizes, LLC, which is doing business as Old Chicago Deli, a restaurant in Green Valley.

Prince Road is an unsecured creditor of the Bonds and is a landlord for a commercial property that the Bonds leased via a different LLC (ITP Enterprizes, LLC) for their Green Valley Furnishings business.

The Bonds filed their petition for relief under Chapter 13 of the United States Bankruptcy Code on December 13, 2011. In their proposed Chapter 13 plan, the Bonds gave Old Chicago a value of $5,000.00: **[*2]** the liquidation value of the used restaurant equipment. Mr. Bond consulted a restaurant equipment vendor for an informal appraisal but did not consult a business broker.

Prince Road filed an objection to the confirmation of the Bonds' Chapter 13 plan, arguing that the Bonds had undervalued their LLCs and that the plan did not treat Prince Road in a fair or reasonable manner because it would pay Prince Road nothing. The Bonds conceded that they planned to continue operation of Old Chicago, but maintained a liquidation value was the proper valuation of their interest in Old Chicago.

After holding an evidentiary hearing on Prince Road's objection to the plan confirmation, Judge Hollowell ordered the Bonds to apply a "going concern"[1] methodology to calculate their 70% interest in Old Chicago, and to amend their plan accordingly. Judge Hollowell explained that she would not confirm the Bonds' original plan because it was inappropriate to apply a liquidation valuation to Old Chicago, and that it

---

[1] "Going-concern" is defined as "the value of the assets of an enterprise considered as an operating business and therefore based on its earning power and prospects rather than on the value of the same assets in the event of liquidation." Merriam-Webster Dictionary, *http://www.merriam-webster.com/dictionary/going-concern%20value*

needed to be treated as an ongoing business. She further stated the Bonds must "calculate a value which reflects what creditors may receive from Debtors' continued possession and operation." (Doc. **[*3]** 17, Ex. L at 8). Judge Hollowell also stated that "the business itself is generating something and it's more than the liquidation value," and that the creditors were "entitled to get as much money as [the Bonds] can get back to them." (Doc. 17, Ex. T at 38).

Judge Hollowell gave the Bonds thirty days to amend their plan. They ultimately chose not to, maintaining their position that the liquidation value was the proper valuation to be used. Judge Hollowell dismissed the case on November 19, 2012.

On November 24, 2012 the Bonds timely filed a notice of appeal to the District Court. They also filed an application to stay dismissal with the bankruptcy court, which was denied. The Bonds then filed a motion for stay with the District Court, which was also denied.

**II. Standard of Review**

Dismissal orders are reviewed for an abuse of discretion, which includes a de novo review **[*4]** of the law and a review of the factual findings for clear error. *See* *In re JTS Corp., 617 F.3d 1102, 1109 (9th Cir. 2010)*; *In re Guastella, 341 B.R. 908, 915 (9th Cir. BAP 2006)*; *In re Stephen, BAP EC-10-1511-DMKPA, 2012 Bankr. LEXIS 1413, 2012 WL 1080455 (B.A.P. 9th Cir. Apr. 2, 2012)*.

**III. Proper Valuation**

The principal issue on appeal is whether the Bonds properly assessed the value of their 70% interest in Old Chicago based on the liquidation value of the restaurant equipment, or whether they were required to apply a going-concern valuation, as ordered by the bankruptcy court.

**a. Law**

In *In re Taffi, 96 F.3d 1190 (9th Cir. 1996)*, the IRS sought to enforce a tax lien on a home that the debtors were going to retain through their plan of reorganization. The Ninth Circuit found that when a Chapter 13 debtor "intends to retain property subject to a lien" and "the proposed use of the property is continued retention by the debtor, the purpose of the valuation is to determine how much the creditor will receive for the debtor's continued possession." *Id. at 1192*.

The Ninth Circuit expanded on *Taffi* in *In re Kim, 130 F.3d 863 (9th Cir. 1997)*. In *Kim*, the debtors filed a Chapter 13 bankruptcy plan treating one claimant **[*5]** as partially secured and the other as wholly secured. The claimants argued the debtors had undervalued the collateral securing their claims. The Ninth Circuit instructed that, "In light of *Taffi*," where the debtors "continue to operate the business ... valuation should be based on the use or disposition to be made of the interest, which in this case means the continued operation of the business in the same location." *Id. at 865*. Thus, the court rejected the debtors' attempt to use the liquidation value of their business equipment because the equipment was not going to be sold, but instead used to sustain an ongoing business. *Id*.

A number of other cases, both from this circuit and others, come to essentially the same conclusion: when a debtor plans to continue operation of a business, the business should be valued as a going concern. *See e.g.* *In re DAK Indus., Inc., 170 F.3d 1197, 1199-1200 (9th Cir. 1999)* (bankruptcy court properly concluded business was a going concern when it continued to operate during the preference period); *In re Tennessee Chemical Co., 143 B.R. 468, 474 (Bankr. E.D. Tenn. 1992)* (court applied going concern value even though business had not made a profit in three **[*6]** years, noting "[g]oing concern value means that value is added to the property because it can be operated as a business."); *In re Thomas, 246 B.R. 500, 505 (E.D.Pa. 2000)* ("liquidation value is not a proper measure of a company ... when the business will continue its operations"); *Matter of Prince, 85 F.3d 314, 319 (C.A.7 (Ill.) 1996)* ("[W]here a business is expected to continue as a going concern, the company's expected future earnings from operations often far exceed the liquidation value of the company's physical assets. Thus, when valuing a business that is continuing to operate as a going concern, liquidation value is generally an inaccurate approximation of what shares are worth to shareholders."); *In re McLaughlin, 217 B.R. 772, 781 (Bankr. W.D.Tex. 1998)*; *Williams v. Swimlear, 2008 WL 1805824 (E.D. N.Y.)*

**b. Parties' Arguments**

The Bonds correctly note that most Chapter 13 cases that consider going concern value focus on "how to

calculate the value of collateral securing a claim proposed to be stripped down" such as in *Kim* and *Taffi*. (Doc. 18 at 11). Thus, the Bonds conclude it is inappropriate to apply a going concern value in their case, because strip down of a secured claim **[*7]** is not at issue. The Bonds further argue that in a hypothetical forced-sale Chapter 7 case, Old Chicago would be worth no more than its used equipment because the Bonds would refuse to sign a non-compete agreement, would refuse to keep running the business, and that Old Chicago is worth nothing without their daily presence.

Prince Road argues that although the Bonds claim they are the only ones capable of successfully operating Old Chicago, and they imply the business isn't worth anything beyond the value of used equipment and therefore no one would buy it, the fact that the Bonds previously sold Old Chicago "proves the business has sale value beyond its liquidation value." (Doc. 22 at 5). Prince Road therefore argues the court's reasoning in cases such as *Thomas* and *Kim* applies here, and that the proper valuation for a business that will continue to operate is the going concern value.

Judge Hollowell acknowledged that most Chapter 13 cases addressing going-concern value focus on calculating the value of collateral securing a claim; however, she also stated the reasoning in those cases extends to the issues at hand here. Judge Hollowell found that although this case concerns an unsecured **[*8]** claim, the proposed liquidation value "ignores that the business is a going concern and that Debtors will operate it." *In re Bond, 2012 Bankr. LEXIS 4107, 2012 WL 3867427 at 4*. Judge Hollowell further stated that "[a]s *Taffi* and *Kim* concluded, this sort of circumstance requires that Debtors calculate a value which reflects what creditors may receive from Debtor's continued possession and operation. That valuation should be calculated on a going-concern basis." *Id*.

**c. Analysis**

It is uncontested that the Bonds plan to continue operation of Old Chicago. The record before the bankruptcy court, as well as the case law reviewed by this Court, supports Judge Hollowell's finding that the Bonds should apply a going concern valuation to Old Chicago. Although there are no cases directly on point to the situation presented here, a number of analogous cases all come to the same conclusion: when a debtor plans to continue operation of a business, the business should be valued as a going concern.

The Court finds Judge Hollowell did not abuse her discretion when she dismissed the Bonds' case after they failed to obey her order instructing them to amend their Chapter 13 plan. "An abuse of discretion may be based on an incorrect **[*9]** legal standard, or a clearly erroneous view of the facts, or a ruling that leaves the reviewing court with a definite and firm conviction that there has been a clear error of judgment." *In re Knedlik, BAP.WW-08-1011-KUKJU, 2008 Bankr. LEXIS 4670, 2008 WL 8444815 (B.A.P. 9th Cir. June 30, 2008)*. None of these situations apply here.

Second, in light of the facts of this case, it was not clearly erroneous for the bankruptcy court to find that the Bonds would continue to conduct business and Old Chicago was, therefore, a going concern. *See In re Greene, 583 F.3d 614, 618 (9th Cir.2009)* (The Court must accept the bankruptcy court's findings of fact unless the Court "is left with the definite and firm conviction that a mistake has been committed.").

Finally, the Court has considered de novo whether the bankruptcy court applied the correct legal standard in ordering the Bonds to apply a going concern valuation, and the Court finds no error here. The cases discussing going concern valuation do not turn on whether the claim is secured or unsecured, as the Bonds argue, but on whether the business will continue or cease operation. The fact that the Bonds plan to continue operating requires a valuation of the business **[*10]** that reflects what Prince Road may receive from the Bonds' continued possession and operation of Old Chicago. The appropriate valuation is, therefore, a going concern valuation.

**IV. Conclusion**

The Bonds' failure to timely file an amended Chapter 13 plan, after a clear order from the bankruptcy court, justified the dismissal of this case. Judge Hollowell was correct when she found Old Chicago to be a going concern, and ordered the Bonds to value it as such. Old Chicago is still a going concern, and it must be treated as one.

Accordingly,

**IT IS HEREBY ORDERED** affirming the Bankruptcy Court's dismissal order. The Clerk shall close its file on this matter.

Dated this 13th day of December, 2013.

/s/ Raner C. Collins

Raner C. Collins

Chief United States District Judge

---

End of Document

# *Taylor v. L.A. County Tax Collector*

United States District Court for the Central District of California

February 7, 2014, Decided; February 7, 2014, Filed

CV 13-09316 BRO (PLAx)

**Reporter**
2014 U.S. Dist. LEXIS 195759 *

JAMES C. TAYLOR, JR. v. LOS ANGELES COUNTY TAX COLLECTOR ET AL.

## Core Terms

motion to dismiss, notice, allegations, documents

**Counsel: [*1]** For Plaintiffs: None.

For Defendants: None.

**Judges:** BEVERLY REID O'CONNELL, United States District Judge.

**Opinion by:** BEVERLY REID O'CONNELL

## Opinion

**CIVIL MINUTES — GENERAL**

**Proceedings: (IN CHAMBERS) RE: DEFENDANT'S MOTION TO DISMISS [6]**

Pending before the Court is Los Angeles County Tax Collector's Motion to Dismiss pursuant to *12(b)(1)* and *12(b)(6) of the Federal Rules of Civil Procedure*. (Dkt. No. 6.) Kay Han filed a Joinder in the Motion to Dismiss. (Dkt. No. 19.) James C. Taylor filed an Opposition. (Dkt. No. 11.) Los Angeles County Tax Collector filed a Reply. (Dkt. No. 12.) After consideration of the papers filed in support of and in opposition to the instant motion, the Court deems this matter appropriate for decision without oral argument. *See Fed. R. Civ. P. 78*; *C.D. Cal. L.R. 7-15*.

This case does not fall under the Court's limited subject matter jurisdiction. Accordingly, the Court **GRANTS** Defendant's Motion to Dismiss **with prejudice**.

**I. BACKGROUND**

On December 18, 2013, Plaintiff James C. Taylor Jr. ("Plaintiff") filed this action against Defendants Los Angeles County Tax Collector ("LA County") and Kay Han ("Ms. Han") (collectively "Defendants"). (Dkt. No. 1.)

This case arises out of the tax auction conducted by LA County of Plaintiff's property. (Compl. ¶ 12.) On October 17, 2012, Plaintiff **[*2]** filed a petition for bankruptcy. Plaintiff alleges that this petition automatically stayed any act of LA County to obtain possession or enforce any lien against his assets. (Compl. ¶ 11.) On October 23, 2012, LA County sold Plaintiff's property located at 4620 Western Avenue, Los Angeles CA, 90062 to Ms. Han. (Compl. ¶ 12.) On November 8, 2012, Plaintiff's bankruptcy petition was denied. (Compl. ¶ 13.)

After the sale was conducted, Ms. Han filed a motion for relief from the automatic stay under *11 U.S.C. § 362*..[1]

---

[1] Defendants ask the Court to take judicial notice of court documents from the action *In re: James Chester Taylor, Jr.*, 2:12-bk-44898. (Dkt. No. 7.) *Federal Rule of Evidence 201* empowers a court to take judicial notice of facts that are either "(1) generally known within the territorial jurisdiction of the trial court; or (2) capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned." *Fed. R. Evid. 201(b)*; *Mullis v. U S. Bankr. Court for Dist. of Nevada, 828 F.2d 1385, 1388 n. 9 (9th Cir.1987)*. The Court **GRANTS** the request for judicial notice of all requested documents. The Court "may take notice of proceedings in other courts, both within and without the federal judicial system, if those proceedings have a direct relation to matters at issue." *U.S. ex rel. Robinson Rancheria Citizens Council v. Borneo, Inc., 971 F.2d 244, 248 (9th Cir. 1992)* (citing *St. Louis Baptist Temple, Inc. v. FDIC, 605 F.2d 1169 (10th Cir. 1979)*). Additionally, Plaintiff incorporates these documents by reference in his Complaint. The "[C]ourt may consider evidence on which the complaint 'necessarily

(Dkt. No. 7.) LA County joined in this motion. On February 28, 2013, the United States Bankruptcy Court issued an order granting relief from the automatic stay under *11 U.S.C. § 362*. (Dkt. No. 7.)

On December 18, 2013, Plaintiff filed the instant Complaint challenging the legality of the tax sale and the validity of the bankruptcy court's February 2013 order. Defendants filed this Motion to Dismiss, arguing that the Court lacks subject matter jurisdiction to review Plaintiff's Complaint and that Plaintiff fails to state a claim.

**II. MOTION TO DISMISS *12(b)(1)***

**A. Federal Question**

A federal court must determine its own jurisdiction even where there is no objection to it. *Rains v. Criterion Systems, Inc., 80 F.3d 339 (9th Cir. 1996)* **[*3]** . Jurisdiction must be determined from the face of the complaint. *Caterpillar, Inc. v. Williams, 482 U.S. 386, 392, 107 S. Ct. 2425, 96 L. Ed. 2d 318 (1987)*. Under *28 U.S.C. § 1331*, federal courts have jurisdiction over "all civil actions arising under the Constitution, laws, or treaties of the United States." *28 U.S.C. §1331*. A case "arises under" federal law if a plaintiff's "well-pleaded complaint establishes either that federal law creates the cause of action" or that the plaintiff's "right to relief under state law requires resolution of a substantial question of federal law in dispute between the parties." *Franchise Tax Bd. v. Constr. Laborers Vacation Trust for S. Cal., 463 U.S. 1, 13, 103 S. Ct. 2841, 77 L. Ed. 2d 420 (1983)*.

Plaintiff alleges that jurisdiction is proper under *28 U.S.C. §§ 1331*, *1334*, *2201*, and *2202*. (Compl. ¶ 1.) In his opposition, Plaintiff does not articulate how these statutes apply to his Complaint or assert any theories involving a federal question. The Court has reviewed the Complaint and finds there is no federal question involved in Plaintiff's allegations. Plaintiff seeks declaratory relief and to quiet title on the property. (Dkt. No. 1.) In both causes of action, Plaintiff is asking the Court to reverse the tax sale conducted by LA County. The rescission of a tax sale is wholly governed by California state law, specifically Revenue and Tax Code *sections 3725* and *3731*. *See Cal. Rev. & Tax. Code §§3725*, *3731*; *see also Van Petten v. Cnty. of San Diego, 38 Cal. App. 4th 43, 46, 44 Cal. Rptr. 2d 816 (1995)* ("A tax sale proceeding is wholly a creature of statute" and "the sole remedies for a purchaser of real property at a tax sale are those provided in the Revenue and Taxation Code.").

Because the issues underlying the controversy between Plaintiff and Defendants—as pled in his Complaint—do not involve any issues of federal law, jurisdiction based on *28 U.S.C. §1331* would be improper.

**B. Diversity**

Original jurisdiction may also be established pursuant to *28 U.S.C. § 1332*. Under *28 U.S.C. § 1332*, a federal district court has **[*4]** "original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $75,000, exclusive of interest and costs, and" the dispute is between "citizens of different states."[2] The Supreme Court has interpreted the statute to require "complete diversity of citizenship," meaning it requires "the citizenship of each plaintiff [to be] diverse from the citizenship of each defendant." *Caterpillar Inc. v. Lewis, 519 U.S. 61, 67-68, 117 S. Ct. 467, 136 L. Ed. 2d 437 (1996)*.

Plaintiff does not invoke jurisdiction under *28 U.S.C. § 1332*. Plaintiff alleges in his Complaint that he and Defendants are citizens of California. (Compl. ¶¶ 4-5.) Accordingly, jurisdiction based on *28 U.S.C. § 1332* is not proper in this case.

**III. MOTION TO DISMISS *12(b)(6)***

**A. Legal Standard**

Under *Rule 8(a)*, a complaint must contain a "short and

---

relies' if (1) the complaint refers to the document; (2) the document is central to the plaintiffs claim; and (3) no party questions the authenticity of the copy attached to the *12(b)(6)* motion." *Marder v. Lopez, 450 F.3d 445, 448 (9th Cir. 2006)* (citations omitted). Such consideration prevents "plaintiffs from surviving a *Rule 12(b)(6)* motion by deliberately omitting reference to documents upon which their claims are based." *Parrino v. FHP, Inc., 146 F.3d 699, 706 (9th Cir. 1998)* (superseded by statute on other grounds as recognized in *Abrego Abrego v. The Dow Chemical Co., 443 F.3d 676, 681-82 (9th Cir. 2006)*).

[2] Diversity of citizenship may also be established on other grounds that are not relevant here. *See 28 U.S.C. § 1332*.

plain statement of the claim showing that the [plaintiff] is entitled to relief." *Fed. R. Civ. P. 8(a)*. If a complaint fails to do this, the defendant may move to dismiss it under *Rule 12(b)(6)*. *Fed. R. Civ. P. 12(b)(6)*. "To survive a motion to dismiss, a complaint must contain sufficient factual matter, accepted as true, to 'state a claim that is plausible on its face.'" *Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S. Ct. 1937, 173 L. Ed. 2d 868 (2009)* (citation omitted) (emphasis added). A claim is plausible on its face "when the plaintiff pleads factual content that allows the court to draw the reasonable **[*5]** inference that the defendant is liable for the misconduct alleged." *Id.* "Factual allegations must be enough to raise a right to relief above the speculative level." *Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 555, 127 S. Ct. 1955, 167 L. Ed. 2d 929 (2007)*. Thus, there must be "more than a sheer possibility that a defendant has acted unlawfully." *Iqbal, 556 U.S. at 678*. "Where a complaint pleads facts that are 'merely consistent with' a defendant's liability, it 'stops short of the line between possibility and plausibility' that the plaintiff is entitled to relief. *Id.*

In ruling on a motion to dismiss for failure to state a claim, a court should follow a two-pronged approach: (1) first, discount conclusory statements, which are not presumed to be true; and then, assuming any factual allegations are true, (2) determine "whether they plausibly give rise to entitlement to relief." *See id. at 679*; *see also Chavez v. U.S., 683 F.3d 1102, 1108 (9th Cir. 2012)*. A court should consider the contents of the complaint and its attached exhibits, documents incorporated into the complaint by reference, and matters properly subject to judicial notice. *Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308, 322-23, 127 S. Ct. 2499, 168 L. Ed. 2d 179 (2007)*; *Lee v. City of Los Angeles, 250 F.3d 668, 688 (9th Cir. 2001)*.

Where a motion to dismiss is granted, a district court should provide leave to amend unless it is clear that the complaint could not be saved by any amendment. *Manzarek v. St. Paul Fire & Marine Ins. Co., 519 F.3d 1025, 1031 (9th Cir. 2008)* (citation omitted).

**B. Discussion**

Even assuming the Court **[*6]** did have subject matter jurisdiction, Plaintiff's Complaint would be untimely. In essence, Plaintiff has "appealed" to this Court an adverse determination against him by United States Bankruptcy Court Judge Vincent P. Zurzolo ("Judge Zurzolo"). (Dkt. No. 7-1.) The court issued its final order in Plaintiff's bankruptcy matter on February 28, 2013. The court ruled that Ms. Han and LA County could "enforce its remedies to foreclose upon and obtain possession of the Property in accordance with applicable nonbankruptcy law." (Dkt. No. 7-1.) Under *Federal Rule of Bankruptcy Procedure 8002(a)*, Plaintiff should have filed any appeal of that order to either the Ninth Circuit Bankruptcy Appellate Panel ("B.A.P.") or the United States District Court within fourteen days. *See F.R.B.P. 8002* ("The notice of appeal shall be filed with the clerk within 14 days of the date of the entry of the judgment, order, or decree appealed from."). Here, Plaintiff did not file his Complaint until December of 2013, over nine months after Judge Zurzolo's order. "The untimely filing of a notice of appeal is jurisdictional." *In Re Souza, 795 F.2d 855, 857 (9th Cir. 1986)* (citations omitted) (reversing district court's decision for lack of jurisdiction based upon untimely notice of appeal). Because it is untimely, **[*7]** the Court lacks jurisdiction to review an appeal of Judge Zurzolo's February 2013 order.

Plaintiff also filed an appeal to the B.A.P., but was similarly denied for untimeliness. (Dkt. No. 7-2.) The court noted that "a timely filed notice of appeal is mandatory and jurisdictional," citing to *Browder v. Director, Department of Corrections, 434 U.S. 257, 264, 98 S. Ct. 556, 54 L. Ed. 2d 521 (1978)*.

Accordingly, the Court finds that review of Judge Zurzolo's order is time-barred.

**IV. CONCLUSION**

In sum, for the reasons discussed above, this Court lacks subject matter jurisdiction over Plaintiff's controversy with Defendants. Accordingly, this action is **DISMISSED with prejudice**.

**IT IS SO ORDERED**.

---

End of Document

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Daniel S. Bleck *(pro hac vice)*
Paul J. Ricotta *(pro hac vice)*
Ian A. Hammel *(pro hac vice)*
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.
Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

Attorneys for Defendant
UMB Bank, N.A. as master indenture trustee

**UNITED STATES BANKRUPTCY COURT**
**CENTRAL DISTRICT OF CALIFORNIA**
**LOS ANGELES DIVISION**

| | |
|---|---|
| In re<br><br>VERITY HEALTH SYSTEM OF CALIFORNIA, INC.<br><br>Debtors and Debtors in Possession.<br>OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., ET AL.,<br>Plaintiffs,<br>v.<br>UMB BANK, NATIONAL ASSOCIATION,<br>Defendant. | Case No.: 2:18-bk-20151-ER<br><br>Adv. No.: 2:19-ap-01166-ER<br><br>**REPLY OF DEFENDANT, UMB BANK, IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT**<br><br>Hearing<br>Date: November 21, 2019<br>Time: 10:00 a.m.<br>Courtroom: 1568<br>Judge: Hon. Ernest M. Robles<br><br>Complaint Filed: June 13, 2019 |

**TABLE OF CONTENTS**

# TABLE OF AUTHORITIES[1]

**Page(s)**

**Cases**



[1] In accordance with Local Rule 9013-2(c)(3)(D), copies of any unpublished decisions cited herein are attached hereto as Exhibit 1.

**Statutes**

Defendant files this reply brief in further support of its Motion to Dismiss the Amended Complaint (the "Motion to Dismiss"), and in response to the *Plaintiff's Opposition to Motion of Defendant UMB Bank, National Association to Dismiss First Amended Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests,* dated October 17, 2019 (the "Opposition"), and respectfully states as follows:[2]

**PRELIMINARY STATEMENT**

Although Plaintiff concedes a number of UMB's arguments made in the Motion to Dismiss, it attempts to substitute equally untenable arguments, presented for the first time in the Opposition, and continues to make claims that are hypothetical and premature.

In the Opposition, Plaintiff concedes that the correct, initial valuation methodology that should be applicable to UMB's Prepetition Collateral is going concern value. That concession should lay to rest any argument that UMB's collateral could be charged with a so-called "going concern premium." Plaintiff's "going concern premium" theory fails unless the initial collateral valuation is made on a liquidation/foreclosure basis. There can be no "going concern premium" if the initial collateral value is determined on a going concern basis.

Plaintiff, however, substitutes an argument that supposedly achieves the same result by asking this Court to rule that going concern value is, essentially, an independent asset class that must be separately listed and described in a valid collateral description. According to Plaintiff, the failure to include phrases such as "going concern value" or "enterprise value" in a collateral description renders it flawed as a matter of law, and prevents a secured creditor from obtaining the full proceeds of a going concern sale. In other words, Plaintiff demands that this Court, once again, strip out any going concern value from UMB's Prepetition Collateral, despite the fact that it admits that going concern value is the correct valuation methodology. This is simply calling Plaintiff's

[2] Capitalized terms used but not defined herein shall have the meanings ascribed to them in *Defendant's Memorandum of Points and Authorities in Support of Defendant's Motion to Dismiss the Amended Complaint,* dated October 1, 2019 [Adv. Pro. Doc.No. 40] (the "Supporting Memorandum").

discredited "going concern premium" argument by another name, and is a collateral attack on controlling precedent in this Circuit.

Plaintiff's new theory is also meritless. Going concern value, enterprise value and the like are just valuation methodologies. They are not separately identifiable classes of assets. They cannot be separated from the underlying assets which generate such value. Perfected security interests are granted by listing and describing assets or categories of assets, not by listing valuation methodologies that may, under certain circumstances, be applied to those assets. Nothing in any secured transactions law or any statute requires a secured creditor to list in its collateral description both the underlying asset as well as all of the possible valuation methodologies that may apply to that asset. Plaintiff is not only wrong on existing law, but it is asking this Court to create new law which would have profoundly significant ramifications.

Plaintiff's remaining Counts should also be dismissed. In its Motion to Dismiss, UMB demonstrated that this Court conclusively found and determined that UMB had an equity cushion in its Prepetition Collateral, and that UMB relied upon such finding in consenting to the priming lien of the DIP Lender. This Court's evidentiary findings as to value have been proven not only to be correct but, based upon the actual Sales Proceeds, a bit understated. The Opposition creates a strawman argument by asserting that Plaintiff should be allowed to continue to challenge any lien in the Debtors' bank accounts and post-petition QAF payments because UMB has made a claim that it currently has a Prepetition Replacement Lien (as defined in the Final DIP Order) on account of an actual diminution in the value of its equity cushion. This is false. UMB has <u>not</u> yet made claim that it has suffered a diminution in the value of its Prepetition Collateral or that it asserts a Prepetition Replacement Lien to protect its equity cushion. UMB expects the Sales Proceeds to repay its secured claim in full without the need to make a claim for diminution in value. Although UMB reserves the right to make such a claim if it is not ultimately paid in full, it has not made such a claim and may never make such a claim. Plaintiff has argued against a phantom claim that is not currently expected to arise, may never arise, is unknown today, and has

not been made by UMB. In short, Plaintiff's arguments in its Opposition are factually incorrect as well as hypothetical and premature.

For all of the reasons set forth in the Supporting Memorandum, as well as those included herein, this Court should dismiss each of the Amended Complaint's four Counts with prejudice.

## ARGUMENT

### I. There Is No Support for Plaintiff's Argument That Going Concern Value Is a Post-Petition Asset That May Be Carved Out from Proceeds of a Going Concern Sale.

Plaintiff has abandoned the original basis for its argument that a so-called "going concern premium" must be carved out from UMB's Prepetition Collateral. Plaintiff originally argued that a premium must be deducted from the value of UMB's secured claim which is equal to the difference between the foreclosure/liquidation value of UMB's Prepetition Collateral and the going concern value of UMB's Prepetition Collateral.[3] Plaintiff now admits, as it must, that the Supreme Court's holding in *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997), as well as controlling Ninth Circuit precedent such as *First Southern Nat'l Bank v. Sunnyslope Hous. L.P. (In re Sunnyslope Hous. L.P.*) 859 F.3d 637, 644 (9th Cir. 2017) (en banc) (citing *In re Taffi*, 96 F.3d 1190, 1192 (9th Cir. 1996) (en banc), *cert. denied*, 138 L. Ed. 2d 987, 117 S. Ct. 2478 (1997)), provide that "going concern value" is the only proper measure for valuing the Prepetition Collateral because the Debtors have always contemplated a going concern sale of their assets. *See* Opposition at 12. Therefore, Plaintiff has conceded that there is no carve-out for any "going concern premium" measured by the difference between the foreclosure or liquidation value of the

[3] Plaintiff asserted that the "bankruptcy process created significant value above what the Defendant ***would have realized upon foreclosure*** on its interest in the Collateral," and that this "going concern premium" is therefore "not the proceeds of the Collateral." *See* Am. Compl. at ¶ 24 (emphasis added). Plaintiff further defined "the going concern premium generated by these Chapter 11 Cases," as "the delta between (i) the prices that would have been paid for the Debtors' assets if the Secured Creditors ***had foreclosed and/or the Debtors ceased operations***, and (ii) the prices generated by the SCC Sale and SGM Sale (together, the "Sales") through these cases[.]" *See Official Committee of Unsecured Creditors' Objection to Motion of the Debtors for an Order Approving Proposed Disclosure Statement and Other Relief [Dkt. 2995]*, dated Sept. 18, 2019 [Docket No. 3092] (the "DS Objection") at 8 (emphasis added).

Prepetition Collateral as of the Petition Date and the going concern value of the Prepetition Collateral as of the date of the Sales.

Despite its concession, Plaintiff continues to assert arguments that directly contradict the rules of *Rash* and *Sunnyslope*. In fact, Plaintiff's new allegations are nothing more than back door attacks on *Rash* and *Sunnyslope*.

For example, Plaintiff has doubled down on its assertion that the Debtors' continuing post-petition operations have "increased" the net realizable value of UMB's collateral during the course of the Debtors' cases. *See* Opposition at 2; 8. Evidently, Plaintiff sees no inconsistency in recognizing that "under the current circumstances, 'going concern value' is the proper measure for ascertaining the value of the Debtor's assets that comprise the 'Prepetition Collateral,'" (Opposition at 12), and simultaneously arguing that there is some "increase" above the going concern value to which UMB is not entitled. The going concern value of the Debtors' assets at the time of the Sales necessarily and, by definition, included the value that was expected to be generated during the pendency of these cases through operating the Hospitals as a going concern. *See, e.g., Bond v. Kerns*, Case No. CV-12-00875-TUC-RCC, 2013 U.S. Dist. LEXIS 184286, *2 n. 1 (D. Ariz. Dec. 16, 2013) (citations and internal quotation marks omitted) ("Going-concern is defined as the value of the assets of an enterprise considered as an operating business and therefore based on its earning power and prospects rather than on the value of the same assets in the event of liquidation."). Plaintiff's continued reference to an "increase" assumes that the starting point for valuation is something lower than going concern value, such as the foreclosure or liquidation value asserted by Plaintiff in the Amended Complaint and in its DS Objection, which theory Plaintiff has been compelled to admit is not supported by applicable case law.

None of the cases cited by Plaintiff in its Opposition supports its argument that some sort of value attributable to the post-petition labor of the Debtors' employees, or the ongoing operation of the Debtors' business, constitutes a separate category of assets, the value of which can be carved out of a secured creditor's secured claim. The absence of such precedent is hardly surprising, since it is a fundamental axiom of valuation methodology that determining the going concern value of

any operating business assumes that it will continue to operate and that labor will continue to be provided by employees working at the business. Plaintiff only cites cases in which courts have reiterated the unremarkable holding that, under Section 552 of the Bankruptcy Code, a prepetition lender's security interest does not extend to new assets created after the petition date. Plaintiff's drastic overstatement of the holdings of inapposite cases is illustrative of the complete lack of support for its position.

Plaintiff's primary authority is a decision from the Bankruptcy Court for the Northern District of Illinois. *HBSC Bank USA v. UAL Corp. (In re UAL Corp.),* 351 B.R. 916 (Bankr. N.D.Ill. 2006). Plaintiff goes so far as to claim that *UAL* is "fatal" to the Motion to Dismiss. *See* Opposition at 13. To the contrary, *UAL Corp.* is completely inapposite. In *UAL Corp.*, the court simply ruled, pursuant to Section 552(b) of the Bankruptcy Code, that the debtor's post-petition negotiation of a 10-year option to extend a lease on real estate that was subject to a prepetition lien was not proceeds of the creditor's prepetition security interest. *Id.* at 924. The debtor's rights in the post-petition, extended lease option were an entirely new asset that did not exist at the time of the filing. Not surprisingly, the court ruled that the prepetition security interest could not extend to an asset which did not even exist as of the petition date. *Id.* at 923. UAL has nothing to do with "going concern value." *UAL* simply holds that, where the debtor obtains a new property right after filing, a prepetition lien does not encumber that new, post-petition asset. That concept has existed since the enactment of the Bankruptcy Code. The *UAL* court simply prohibited the secured creditor from claiming an increase to its collateral value as a result of the debtor's acquisition of post-petition property rights. In this case, UMB is not claiming any increase in the value of its prepetition lien after the Petition Date on account of the Debtors' acquisition of any new assets. As explained in detail in the Supporting Memorandum, this Court has already found that, as of the Petition Date, UMB is oversecured on a going concern basis. UMB does not seek to increase that valuation and, most likely, UMB's collateral has not, in fact, increased in value since the Petition Date, especially in light of the undisputed fact that the Debtors have been losing approximately $450,000 per day. *See* Supplemental Cash Collateral Motion at ¶ 15.

The balance of the cases cited by Plaintiff similarly fail to support Plaintiff's position, as none of them establish an independent category of collateral that may be separated and carved out from proceeds of a going concern sale. At best, they simply acknowledge that, under Section 552, post-petition assets are not subject to prepetition liens. None of the cases even intimate that "going concern value" constitutes a separate category of assets that may be stripped from the underlying asset. For example, Plaintiff's reliance on *In re Cafeteria Operators, L.P.*, 299 B.R. 400 (Bankr. N.D. Tex. 2003) as "equally fatal" to UMB's position is unavailing. *Cafeteria Operators* simply ruled that, when proceeds arise from a sale of assets that include both collateral and unencumbered property, the portion of the proceeds derived from the sale of the unencumbered assets do not constitute lien proceeds. *Id.* at 410. The court authorized the debtors to utilize the lender's cash collateral over its objection, and granted the lender a replacement lien on all of the debtor's assets. *Id. Cafeteria Operators* contains no discussion of a "going concern value" at all, let alone does it identify such value as a separate category of assets that may be stripped from the underlying assets. Likewise, in *Far East Nat'l Bank v. United States Tr. (In re Premier Golf Props., LP),* 477 B.R. 767 (B.A.P. 9th Cir. 2012), the court determined that greens fees and driving range fees are not the rents, proceeds or profits of the lender's prepetition security interest. There is no discussion of carving out going concern value from the collateral. Moreover, there are no such assets involved in the Debtors' bankruptcy proceedings. The Committee also relies on *Arkison v. Frontier Asset Mgmt., LLC (In re Skagit Pac. Corp.),* (B.A.P. 9th Cir. 2004), in which the court determined that an account receivable generated post-petition is not proceeds of the lender's prepetition security interest in receivables. Once again, this has nothing to do with stripping off going concern value from the underlying asset. In fact, *Skagit* undercuts Plaintiff's argument because the court did note that its analysis would change if "the court grants a replacement lien in any new post-petition accounts receivable[.]" *Id.* at 337. UMB has, in fact, been granted a replacement lien by virtue of the Final DIP Order in this case.

Plaintiff's characterization of *In re Ebbler Furniture & Appliances, Inc.*, 804 F.2d 87 (7th Cir. 1986) is misleading and inaccurate. The *Ebbler* Court was asked to define the word "value"

as used in Section 547(c)(5) of the Bankruptcy Code, which section prevents a secured creditor from improving its position at the expense of an unsecured creditor during the 90 days prior to filing the bankruptcy petition. *Id.* at 89. Noting that other definitions of "value" provided by the Bankruptcy Code would not be useful for Section 547(c)(5) purposes, the Seventh Circuit found that the bankruptcy court appropriately utilized "cost basis" as the method for valuing the collateral. *Id.* at 90. Thus, the holding of *Ebbler* has absolutely nothing to do with the issues in this case. In its Opposition, Plaintiff merely cites to Judge Easterbrook's concurring opinion. Not only is a Seventh Circuit decision from 1986 not controlling on this Court, but Judge Easterbrook's concurring remarks are nothing more than *dicta*, even in the Seventh Circuit.

Plaintiff also cites *Ardmor Vending Co. v. Kim (In re Kim)*, 130 F.3d 863 (9th Cir. 1997) as though it somehow supports its argument. It does not. In *Kim,* the debtor intended to continue to operate its dry cleaning business using the secured creditors' collateral. The Ninth Circuit reversed the holdings of the B.A.P. and the bankruptcy court because they improperly valued the prepetition secured creditors' collateral (a lease and certain equipment) based on a liquidation value rather than as a turn-key operation. Because the debtor proposed to continue to use the property, a valuation on a going concern basis indicated that the secured creditors were fully secured in the entire enterprise value of the business. *Id.* at 866. Far from supporting Plaintiff's argument, *Kim* supports UMB's position that the value of the Prepetition Collateral must be determined by its going concern value. Plaintiff likewise misstates *In re 26 Trumbull Street*, 77 B.R. 374 (Bankr. D. Conn. 1987). Contrary to the Committee's misleading parenthetical in its Opposition (Opposition at 16), nowhere in this two page decision does the court opine on, let alone allocate, anything described as "going concern value." Rather, the court agreed with the secured creditor's valuation methodology of the collateral, and allocated the sales proceeds among the assets, based upon which assets were subject to the secured creditor's lien and which were not. *Id.* at 375.

It is notable that Plaintiff is unable to identify any precedent, in this circuit or others, that would support its theory. Instead, Plaintiff can only cite academic articles, despite its assertion

that its argument is not purely academic. *See* Opposition at 15 n. 9.

**II. Plaintiff's "Going Concern Premium" Argument Conflates Valuation Methodologies with Asset Categories, and Asks This Court to Create New Law Holding that "Going Concern Value" Constitutes a Separately Identifiable Category of Assets That Must Be Included in a Collateral Description in Order to Establish a Perfected Lien**

In its Opposition, Plaintiff conflates two distinct concepts: valuation methodology and asset categorization. "Going concern value" is a valuation methodology, not a category of assets. Assets include items such as real property, accounts, machinery and equipment, contract or license rights, etc. Valuation methodologies describe how such assets may be assigned a value. There is no requirement in any real estate law or in the Uniform Commercial Code (the "UCC") to include in the collateral description all conceivable valuation methodologies that may subsequently be applied to value that collateral. The only requirement for attachment and perfection of a lien is to list or describe the assets themselves either by asset, or by category of asset. In fact, the UCC does not mention valuation methodology when it specifies the requirements for a proper collateral description. *See* UCC Section 9-109(a) ("[Article 9 of the UCC] apples to: (1) a transaction, regardless of its form, that creates a security interest in personal property or fixtures by contract;"); UCC Section 9-108(a) ("a description of personal or real property is sufficient whether or not it is specific, if it reasonably identifies what is described").

As explained by the Supreme Court in *Rash*, an asset may have a number of different valuations, depending on the debtors' use or disposition of the asset. *See Rash,* 520 U.S. at 962-63. One of those valuations is going concern value. But, it is the same asset that generates those different valuations, not a separate and distinct category of asset called "going concern value." Simply put, a valuation methodology is not an asset that can be subject to a separate lien; it is simply the value of an asset, and it is the asset, not the valuation methodology, which is the collateral subject to the rules and requirements of perfection. As noted in UMB's Motion to Dismiss, and as conceded in the Opposition, Plaintiff has not challenged the fact that UMB has satisfied the requirement for perfection (other than with respect to certain bank accounts and post-petition QAF payments).

Plaintiff has not cited – and cannot cite - one case that stands for the proposition that "going concern value" is a distinct type or category of asset that must be separately described in a collateral description in order to perfect a lien. That proposition also makes no logical sense. If "going concern" or "enterprise" value were a separate category of collateral under the UCC, it could theoretically be sold separately and apart from the underlying asset. Further, if this Court were to adopt Plaintiff's argument, it would be tantamount to establishing new law applicable to all secured transactions: in order to be entitled to the full sale proceeds arising from the sale of a debtor's collateral that is being sold on a going concern basis, the secured lender would need to include words such as "going concern" or "enterprise value" as a distinct category of assets in the collateral description in its mortgage or UCC-1 financing statement.

Plaintiff is simply wrong on the law. But, solely for the sake of argument, even if there does exist a separate category of assets and collateral known as "going concern value," UMB would have a perfected lien. Plaintiff's mythical asset class could only be encompassed by the UCC collateral category denoted as "intangibles." Plaintiff could not possibly argue that "going concern value" is a tangible asset. *See* UCC Section 9-102(42) (definition of "General Intangibles"). Since UMB's collateral description does include "intangibles," UMB would have a perfected lien in "going concern value," even assuming Plaintiff's theory has any merit whatsoever. *See* Supporting Memorandum at 5-6 (describing UMB's security interest as including intangibles).

Last, Plaintiff appears to acknowledge the invalidity of its own argument. In footnote 6 on page 13 of the Opposition, Plaintiff states that it

> has not objected, and would not object, to the Debtors, and the Court, adopting a 'going concern value' metric for all relevant purposes, including 'valuation' of the Prepetition Liens and Prepetition Obligation, so long as any amounts attributable to Debtors' assets as to which the UMB Secured Creditors have not been able to establish valid, perfected, and enforceable liens is deducted from the value of Prepetition Liens and Prepetition Obligation for distribution purposes.

Plaintiff's offer to limit this litigation and to value all collateral based only a going concern basis is a constructive step in the right direction. UMB interprets such an offer to mean that Plaintiff's lien challenge will no longer include any attempts to carve out any going concern value on any basis whatsoever from UMB's secured claim, including any substitute basis argued in the Opposition, and that Plaintiff's claims are now limited, as presented in the Initial Complaint, to a challenge with respect to the perfection of UMB's liens on (i) the Debtors' prepetition bank accounts, and (ii) the Debtors' rights in payments arising from post-petition QAF cycles (*viz.*, QAF cycles 6 – 10).

**III. Contrary to Plaintiff's Representations, UMB is Not Currently Asserting A Prepetition Replacement Lien; Therefore, Counts II and III Are Premature and Fail to Present a Case or Controversy.**

In its Motion to Dismiss, UMB argues that Plaintiff's lien challenge with respect to UMB's security interest in the Debtors' Deposit Accounts[4] is moot because all of the funds in those accounts have long since been used and expended by the Debtors to fund their significant cash flow operating losses. Plaintiff admits that all such funds are now gone. *See* Opposition at 17. This should render Plaintiff's lien challenge with respect to the Deposit Accounts moot. Plaintiff argues, however, that its challenge to UMB's security interest in the Deposit Accounts continues to be relevant because UMB presently contends that it will have a diminution claim, and the extent of UMB's prepetition liens in the Deposit Accounts will need to be determined in order to calculate the amount of such diminution. *Id.* Plaintiff factually misstates UMB's position. While UMB would be entitled to a Prepetition Replacement Lien pursuant to the express terms of the Final DIP Order that would encumber **all** of the Debtors' assets to the extent of any diminution in the value of its Prepetition Collateral, UMB is not currently asserting that there is any diminution in value. UMB reserves the right to make such a claim in the future if it is not paid in full but, at present, UMB expects to be fully paid if the remaining Hospital sale closes on a timely basis and on its

[4] As defined in the Amended Complaint.

current terms. In fact, UMB has consistently maintained that it is oversecured, based both on this Court's findings in connection with the Final DIP Order and as confirmed by the fact that the actual Sales Proceeds are expected to exceed UMB's secured claim by an even greater margin. *See* Supporting Memorandum at 9; 19-21. The Sales may also result in excess Sales Proceeds that would inure to the benefit of the unsecured creditors. Therefore, Plaintiff's argument that Count II of the Amended Complaint should survive because UMB is currently claiming a Prepetition Replacement Lien due to a diminution in value is simply wrong as matter of fact and is, at best, hypothetical and premature. Count II should be dismissed because it presents no current case or controversy.

In Count III of the Amended Complaint, Plaintiff seeks to invalidate any lien on post-petition QAF (*viz*., QAF Payments received on account of QAF Cycles 6 – 10). Once again, solely for purposes of the Motion to Dismiss and reserving all rights, UMB is not currently asserting a Prepetition Replacement Lien on post-petition QAF Payments, because UMB expects to be paid in full from the Sales Proceeds. Thus, UMB may never need to assert any diminution claim resulting in a Prepetition Replacement Lien. Accordingly, like the relief sought in Count II, the relief sought in Count III is hypothetical, premature and fails to present a case or controversy.

Finally, it should also be noted that Plaintiff's assertion that the funds held in the Deposit Accounts "have been consumed in running the Hospitals, thus benefiting the UMB Secured Creditors, when those funds could instead have been made available to unsecured creditors" (Opposition at 17) attempts to turn reality on its head. If Plaintiff genuinely believed that it was in its constituency's best interest for the Debtors to immediately liquidate so that it could have had access to the Deposit Accounts, it had every opportunity to seek appropriate relief in this Court. Plaintiff voluntarily chose not to do so. Instead, Plaintiff allowed these cases to be fully funded and paid for by the Prepetition Secured Creditors in the hopes that the continued operation of the Hospitals, including the use of the cash in the Deposit Accounts, would afford the unsecured creditors the possibility for a greater recovery than if the Hospitals were shuttered and the cash

were distributed. Plaintiff took the risk. It should not now be entitled to charge UMB with the downside cost of its own gamble.

**IV. Plaintiff Is Not Entitled to Attack Any and All Aspects of UMB's Secured Claim Well After the Expiration of the Challenge Deadline Based on the Word "Including" in Count I of the Amended Complaint**

Plaintiff makes the untenable argument that, despite the expiration of the Challenge Deadline, by qualifying Count I with the word "including," it is entitled to challenge additional categories of UMB's collateral that are not specifically enumerated in the Amended Complaint. *See* Opposition at 5; 21. Plaintiff's argument would create a secret Lien Challenge and eviscerate federal pleading standards which require that defendants be "provided fair notice of the claim being asserted and the grounds upon which it rests." *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544, 570 (2007). The case cited by Plaintiff in support of its position does not hold differently. In *In re Kline,* the court allowed plaintiff to amend its complaint to include a specific bank account as an "additional example" of an asset that was allegedly fraudulently transferred, the existence of which debtor hid from plaintiff. No. 8:13-bk-11334-TA, 2014 WL 12665719, at *2 (Bankr. C.D. Cal. Mar. 11, 2014). Neither *Kline,* nor any other case cited by Plaintiff, can support the outlandish position that by simply using the word "including" in a complaint, a plaintiff is free to continue to add additional facts and causes of action well past the Challenge Deadline. If Plaintiff is allowed to maintain that Count I of the Amended Complaint merely contains a "non-exhaustive list of assets in which the UMB Secured Creditors do *not* have a lien," (Opposition at 3), when is Plaintiff ever required to provide an exhaustive list? By filing a lien challenge by the deadline, Plaintiff should not be given *carte blanche* subsequently to prosecute any lien challenge.

## CONCLUSION

For the reasons stated above, as well as those set forth in the Supporting Memorandum, each of the Counts of the Amended Complaint should be dismissed, with prejudice.

DATED: October 24, 2019

MINTZ LEVIN COHN FERRIS GLOVSKY AND POPEO, P.C.

Daniel S. Bleck (*pro hac vice*)
Paul J. Ricotta (*pro hac vice*)
Ian A. Hammel (*pro hac vice*)
One Financial Center
Boston, MA 02111
Tel: 617-542-6000
Fax: 617-542-2241
Email: dsbleck@mintz.com
Email: pjricotta@mintz.com
Email: iahammel@mintz.com

-and-

Abigail V. O'Brient (SBN 265704)
2029 Century Park East, Suite 3100
Los Angeles, CA 90067
Tel: 310-586-3200
Fax: 310-586-3202
Email: avobrient@mintz.com

*Attorneys for UMB Bank, N.A. as master indenture trustee*

# EXHIBIT 1

# Bond v. Kerns

United States District Court for the District of Arizona

December 13, 2013, Decided; December 16, 2013, Filed

No. CV-12-00875-TUC-RCC

**Reporter**
2013 U.S. Dist. LEXIS 184286 *; 2013 WL 7046375

Mark Bond and Ashlea Bond, Appellants, v. Dianne C. Kerns, et al., Appellees.

**Prior History:** *In re Bond, 2012 Bankr. LEXIS 4107 (Bankr. D. Ariz., Sept. 5, 2012)*

## Core Terms

valuation, liquidation value, cases, bankruptcy court, calculate

**Counsel:** **[*1]** For Mark Bond, Debtors, Ashlea Bond, Debtors, Appellants: H Lee Horner, Jr., LEAD ATTORNEY, Goldstein Horner & Horner Attorneys, Cortaro, AZ.

Dianne C Kerns, Chapter 13, Trustee, Appellee, Pro se, Tucson, AZ.

For Prince Road Associated LLC, Appellee: Karl E MacOmber, LEAD ATTORNEY, Monroe & McDonough PC, Tucson, AZ.

**Judges:** Raner C. Collins, Chief United States District Judge.

**Opinion by:** Raner C. Collins

## Opinion

**ORDER**

Pending before the Court is Appellants' appeal from the Bankruptcy Court's dismissal of their Chapter 13 case. This matter has been fully briefed, and the Court heard oral arguments on December 12, 2013. For the following reasons, the Court will dismiss the appeal.

**I. Background**

The Bonds have a 70% interest in AMG Enterprizes, LLC, which is doing business as Old Chicago Deli, a restaurant in Green Valley.

Prince Road is an unsecured creditor of the Bonds and is a landlord for a commercial property that the Bonds leased via a different LLC (ITP Enterprizes, LLC) for their Green Valley Furnishings business.

The Bonds filed their petition for relief under Chapter 13 of the United States Bankruptcy Code on December 13, 2011. In their proposed Chapter 13 plan, the Bonds gave Old Chicago a value of $5,000.00: **[*2]** the liquidation value of the used restaurant equipment. Mr. Bond consulted a restaurant equipment vendor for an informal appraisal but did not consult a business broker.

Prince Road filed an objection to the confirmation of the Bonds' Chapter 13 plan, arguing that the Bonds had undervalued their LLCs and that the plan did not treat Prince Road in a fair or reasonable manner because it would pay Prince Road nothing. The Bonds conceded that they planned to continue operation of Old Chicago, but maintained a liquidation value was the proper valuation of their interest in Old Chicago.

After holding an evidentiary hearing on Prince Road's objection to the plan confirmation, Judge Hollowell ordered the Bonds to apply a "going concern"[1] methodology to calculate their 70% interest in Old Chicago, and to amend their plan accordingly. Judge Hollowell explained that she would not confirm the Bonds' original plan because it was inappropriate to apply a liquidation valuation to Old Chicago, and that it

---

[1] "Going-concern" is defined as "the value of the assets of an enterprise considered as an operating business and therefore based on its earning power and prospects rather than on the value of the same assets in the event of liquidation." Merriam-Webster Dictionary, *http://www.merriam-webster.com/dictionary/going-concern%20value*

needed to be treated as an ongoing business. She further stated the Bonds must "calculate a value which reflects what creditors may receive from Debtors' continued possession and operation." (Doc. **[*3]** 17, Ex. L at 8). Judge Hollowell also stated that "the business itself is generating something and it's more than the liquidation value," and that the creditors were "entitled to get as much money as [the Bonds] can get back to them." (Doc. 17, Ex. T at 38).

Judge Hollowell gave the Bonds thirty days to amend their plan. They ultimately chose not to, maintaining their position that the liquidation value was the proper valuation to be used. Judge Hollowell dismissed the case on November 19, 2012.

On November 24, 2012 the Bonds timely filed a notice of appeal to the District Court. They also filed an application to stay dismissal with the bankruptcy court, which was denied. The Bonds then filed a motion for stay with the District Court, which was also denied.

**II. Standard of Review**

Dismissal orders are reviewed for an abuse of discretion, which includes a de novo review **[*4]** of the law and a review of the factual findings for clear error. *See* *In re JTS Corp., 617 F.3d 1102, 1109 (9th Cir. 2010)*; *In re Guastella, 341 B.R. 908, 915 (9th Cir. BAP 2006)*; *In re Stephen, BAP EC-10-1511-DMKPA, 2012 Bankr. LEXIS 1413, 2012 WL 1080455 (B.A.P. 9th Cir. Apr. 2, 2012)*.

**III. Proper Valuation**

The principal issue on appeal is whether the Bonds properly assessed the value of their 70% interest in Old Chicago based on the liquidation value of the restaurant equipment, or whether they were required to apply a going-concern valuation, as ordered by the bankruptcy court.

**a. Law**

In *In re Taffi, 96 F.3d 1190 (9th Cir. 1996)*, the IRS sought to enforce a tax lien on a home that the debtors were going to retain through their plan of reorganization. The Ninth Circuit found that when a Chapter 13 debtor "intends to retain property subject to a lien" and "the proposed use of the property is continued retention by the debtor, the purpose of the valuation is to determine how much the creditor will receive for the debtor's continued possession." *Id. at 1192*.

The Ninth Circuit expanded on *Taffi* in *In re Kim, 130 F.3d 863 (9th Cir. 1997)*. In *Kim*, the debtors filed a Chapter 13 bankruptcy plan treating one claimant **[*5]** as partially secured and the other as wholly secured. The claimants argued the debtors had undervalued the collateral securing their claims. The Ninth Circuit instructed that, "In light of *Taffi*," where the debtors "continue to operate the business ... valuation should be based on the use or disposition to be made of the interest, which in this case means the continued operation of the business in the same location." *Id. at 865*. Thus, the court rejected the debtors' attempt to use the liquidation value of their business equipment because the equipment was not going to be sold, but instead used to sustain an ongoing business. *Id*.

A number of other cases, both from this circuit and others, come to essentially the same conclusion: when a debtor plans to continue operation of a business, the business should be valued as a going concern. *See e.g.* *In re DAK Indus., Inc., 170 F.3d 1197, 1199-1200 (9th Cir. 1999)* (bankruptcy court properly concluded business was a going concern when it continued to operate during the preference period); *In re Tennessee Chemical Co., 143 B.R. 468, 474 (Bankr. E.D. Tenn. 1992)* (court applied going concern value even though business had not made a profit in three **[*6]** years, noting "[g]oing concern value means that value is added to the property because it can be operated as a business."); *In re Thomas, 246 B.R. 500, 505 (E.D.Pa. 2000)* ("liquidation value is not a proper measure of a company ... when the business will continue its operations"); *Matter of Prince, 85 F.3d 314, 319 (C.A.7 (Ill.) 1996)* ("[W]here a business is expected to continue as a going concern, the company's expected future earnings from operations often far exceed the liquidation value of the company's physical assets. Thus, when valuing a business that is continuing to operate as a going concern, liquidation value is generally an inaccurate approximation of what shares are worth to shareholders."); *In re McLaughlin, 217 B.R. 772, 781 (Bankr. W.D.Tex. 1998)*; *Williams v. Swimlear, 2008 WL 1805824 (E.D. N.Y.)*

**b. Parties' Arguments**

The Bonds correctly note that most Chapter 13 cases that consider going concern value focus on "how to

calculate the value of collateral securing a claim proposed to be stripped down" such as in *Kim* and *Taffi*. (Doc. 18 at 11). Thus, the Bonds conclude it is inappropriate to apply a going concern value in their case, because strip down of a secured claim **[*7]** is not at issue. The Bonds further argue that in a hypothetical forced-sale Chapter 7 case, Old Chicago would be worth no more than its used equipment because the Bonds would refuse to sign a non-compete agreement, would refuse to keep running the business, and that Old Chicago is worth nothing without their daily presence.

Prince Road argues that although the Bonds claim they are the only ones capable of successfully operating Old Chicago, and they imply the business isn't worth anything beyond the value of used equipment and therefore no one would buy it, the fact that the Bonds previously sold Old Chicago "proves the business has sale value beyond its liquidation value." (Doc. 22 at 5). Prince Road therefore argues the court's reasoning in cases such as *Thomas* and *Kim* applies here, and that the proper valuation for a business that will continue to operate is the going concern value.

Judge Hollowell acknowledged that most Chapter 13 cases addressing going-concern value focus on calculating the value of collateral securing a claim; however, she also stated the reasoning in those cases extends to the issues at hand here. Judge Hollowell found that although this case concerns an unsecured **[*8]** claim, the proposed liquidation value "ignores that the business is a going concern and that Debtors will operate it." *In re Bond, 2012 Bankr. LEXIS 4107, 2012 WL 3867427 at 4*. Judge Hollowell further stated that "[a]s *Taffi* and *Kim* concluded, this sort of circumstance requires that Debtors calculate a value which reflects what creditors may receive from Debtor's continued possession and operation. That valuation should be calculated on a going-concern basis." *Id*.

**c. Analysis**

It is uncontested that the Bonds plan to continue operation of Old Chicago. The record before the bankruptcy court, as well as the case law reviewed by this Court, supports Judge Hollowell's finding that the Bonds should apply a going concern valuation to Old Chicago. Although there are no cases directly on point to the situation presented here, a number of analogous cases all come to the same conclusion: when a debtor plans to continue operation of a business, the business should be valued as a going concern.

The Court finds Judge Hollowell did not abuse her discretion when she dismissed the Bonds' case after they failed to obey her order instructing them to amend their Chapter 13 plan. "An abuse of discretion may be based on an incorrect **[*9]** legal standard, or a clearly erroneous view of the facts, or a ruling that leaves the reviewing court with a definite and firm conviction that there has been a clear error of judgment." *In re Knedlik, BAP.WW-08-1011-KUKJU, 2008 Bankr. LEXIS 4670, 2008 WL 8444815 (B.A.P. 9th Cir. June 30, 2008)*. None of these situations apply here.

Second, in light of the facts of this case, it was not clearly erroneous for the bankruptcy court to find that the Bonds would continue to conduct business and Old Chicago was, therefore, a going concern. *See In re Greene, 583 F.3d 614, 618 (9th Cir.2009)* (The Court must accept the bankruptcy court's findings of fact unless the Court "is left with the definite and firm conviction that a mistake has been committed.").

Finally, the Court has considered de novo whether the bankruptcy court applied the correct legal standard in ordering the Bonds to apply a going concern valuation, and the Court finds no error here. The cases discussing going concern valuation do not turn on whether the claim is secured or unsecured, as the Bonds argue, but on whether the business will continue or cease operation. The fact that the Bonds plan to continue operating requires a valuation of the business **[*10]** that reflects what Prince Road may receive from the Bonds' continued possession and operation of Old Chicago. The appropriate valuation is, therefore, a going concern valuation.

**IV. Conclusion**

The Bonds' failure to timely file an amended Chapter 13 plan, after a clear order from the bankruptcy court, justified the dismissal of this case. Judge Hollowell was correct when she found Old Chicago to be a going concern, and ordered the Bonds to value it as such. Old Chicago is still a going concern, and it must be treated as one.

Accordingly,

**IT IS HEREBY ORDERED** affirming the Bankruptcy Court's dismissal order. The Clerk shall close its file on this matter.

Dated this 13th day of December, 2013.

/s/ Raner C. Collins

Raner C. Collins

Chief United States District Judge

---

End of Document

2014 WL 12665719
Only the Westlaw citation is currently available.
United States Bankruptcy Court, C.D. California, Santa Ana Division.

IN RE: Dennis P. KLINE, Debtor.
Pride Mobility Products Corporation, Plaintiff,
v.
Dennis P. Kline, Defendant.

Case No.: 8:13–bk–11334–TA
|
Adv. No. 8:13–ap–01250–TA
|
Signed March 11, 2014
|
Date: February 6, 2014, Time: 11:00 a.m., Location: Courtroom 5B

**Attorneys and Law Firms**

BRADLEY D. BLAKELEY (SBN 189756), Email: bblakeley@blakeleyllp.com, DAVID M. MANNION (SBN 288627), E–Mail: dmannion@blakeleyllp.com, BLAKELEY & BLAKELEY LLP, 2 Park Plaza, Suite 400, Irvine, California 92614, Telephone: (949) 260–0611, Facsimile: (949) 260–0613, Attorneys for Plaintiff, Pride Mobility Products Corporation

**ORDER DENYING DEFENDANT'S MOTION TO DISMISS PLAINTIFF'S FIRST AMENDED COMPLAINT**

Theodor C. Albert, United States Bankruptcy Judge

***1** Defendant Dennis P. Kline's *Motion to Dismiss the First Amended Complaint* having been considered, for reasons set forth in the tentative ruling, and good cause appearing,

IT IS ORDERED as follows:

This is the defendant's motion to dismiss the First Amended Complaint under Rule 12(b)(6). The complaint is one objecting to discharge under 11 U.S.C. §§ 727(a) (2)(3)(4a)(A) and (5). Thethrust of the motion is that: (1) although the original complaint was timely, the amended complaint raises new facts and issues which are not sufficiently related to the original complaint so as to "relate back," and since the original complaint was filed on the last possible day, the new portions of the complaint must be dismissed with prejudice on limitations grounds; and (2) even if the new material did relate back, it still is not stated with sufficient detail to pass muster under Rule 9. Most of the new material relates to an alleged account at Citibank which debtor reportedly failed to list on his schedules, failed to reveal at the § 341a meeting, failed to reveal despite repeated discovery requests and which was material considering it contained many thousands both before and after the petition date.

First, the court must dispose of the plaintiff's arguments based on equitable tolling, equitable estoppel or exercise of some similar, vague powers under § 105. Because these principles have to be exercised only to the extent not inconsistent with plain language of specific rules, and the purposes served by those rules, they are largely unavailing in discharge and dischargeability matters. *Schunk v. Santos (In re Santos)*, 112 B.R. 1001, 1006–08 (9th Cir. BAP 1990). This is because FRBP 4004(a) and (b), 4007(c) and 9006(b)(3) carefully specify that the limitations can only be extended by court order within the original time period. The limitations are strictly construed in the Ninth Circuit and are not susceptible to expansion for equitable reasons or under § 105. *Id.*; see also *Kamjoo v. Wright ( In re Wright)*, 2010 WL 6259968 (9th Cir BAP 2010).

But a closer question is whether there is any need for resort to equitable remedies. Plaintiff contends the amendments relate back to the original, timely-filed complaint. Plaintiff argues that the purpose of Rule 15 [governing amendments] is to facilitate decisions on the merits rather than pleadings or technicalities, and is applied more leniently when amendments are only against a single defendant and not adding additional parties. *United States ex rel. Cericola v. FNMA*, 529 F.Supp.2d 1139, 1148 (C.D. Cal. 2007), citing *Martell v. Trilogy, Ltd.*, 872 F.2d 322, 324 (9th Cir. 1989). The "relation back" standard of Rule 15 (c) is articulated in defendant's cited case *Gelling v. Dean (In re Dean)*, 11 B.R. 542, 545 (9th Cir. BAP 1981), *aff'd* 687 F.2d 307 (9th Cir. 1982): "In determining whether an amended cause of action is to relate back, the emphasis is not on the legal theory of the action, but whether the specified conduct of the defendant, upon which the plaintiff is relying to enforce his amended claim, is identifiable with the original claim. (*Citing* 3 Moore's Federal Practice ¶ 15.15(3) pp. 15–196–205 (2d ed. 1980)). The basic test is whether the evidence with respect to the second set of allegations could have been introduced under the original complaint liberally construed;

or as a corollary, that in terms of notice, one may fairly perceive some identification or relationship between what was pleaded in the original and amended complaints." citing *Rural Fire Protection Co. v. Hepp*, 366 F.2d 355 (9th Cir. 1966).

***2** The original complaint contains allegations regarding ownership of RSL, accounts in the Cook Islands, sales of watches and reference is made to a safety deposit at Chase Bank, and a wine collection only disclosed post-petition. ¶¶ 81–103. The plaintiff in the original complaint observes a marked discrepancy between a prepetition financial statement and the amounts listed on the schedules, suggesting missing assets. ¶ 84–85 and 88–89, 91. Similarly, the plaintiff in the complaint notes that the loss of Source One's (debtor's corporation) assets is unexplained. ¶¶ 104–111. No specific reference is made to an account at Citibank. However, the stated facts are all by reference run through the more expansive charging allegation of the First Claim for Relief found at ¶ 113: "The debtor has, with intent to hinder, delay, or defraud his creditors, transferred, removed or concealed property within one year prior to filing the Bankruptcy Petition, ***including*** by selling his shares in RSL and using the Cook Islands Trust to conceal assets." (emphasis added) So the alleged specific instances of transfers and concealments, though not including reference to Citibank, are specifically not made exclusive, but only exemplary. A similar analysis could be done for the Second Claim for Relief and use of the word "including" at ¶ 116 as well as the incorporation of all preceding paragraphs in ¶ 115. So, adopting the *Dean* standard, the court has little doubt that evidence of a hidden and omitted bank account at Citibank would be admissible concerning the First and the Second Claims for Relief "liberally construed."

Moreover, the court views the teaching of *Cericola* as instructive here. The relator plaintiff in *Cericola* outlined in her original timely complaint a scheme to defraud the government by FNMA's procurement of insurance on loans not qualified for HUD insurance. The original complaint was woefully short of details on the specific loans in question, but nevertheless the court viewed the original complaint sufficient for relation back purposes (and thus avoiding a limitations issue) because it put the defendant on notice as to the general outlines of the scheme. 529 F.Supp.2d at 1149. Similarly, in the case at bar, no doubt the plaintiff would have originally mentioned Citibank had it known of same. But that does not mean that there is not sufficient notice of the more general failure to account for assets and attempts to hinder, delay and defraud creditors and conceal from the trustee and creditors the defendant's assets.

Defendant's authorities are largely distinguishable. *In re Magno,* 216 B.R. 34 (9th Cir. BAP 1997) involved the question of whether a § 523 theory of relief was a "lesser included" offense within a timely-filed § 727 complaint. The BAP correctly determined there was little connection between the elements of an individual fraud theory and the more general intent to hinder, delay or defraud and/or a false oath in the case. *Id.* at 42. Somewhat closer, but still not persuasive, is *Stodd v. Mufti (In re Mufti)*, 61 B.R. 514 (Bankr. C.D.Cal. 1986). In *Mufti,* the facts alleged in the original timely complaint concerned a fraudulent pre-petition transfer of real estate, but this did not sufficiently relate to amended (and untimely) allegations concerning fraudulent concealment of same. This is logical: the original complaint dealt with a prepetition *transfer* that was fraudulent as to creditors; the second theory necessarily related to a post-petition failure to *testify* truthfully regarding same, an entirely different theory. But here, the undisclosed Citibank account is only *an additional example* of what has already been alleged regarding prepetition attempts to conceal or transfer assets out of the reach of creditors and failures post-petition to account in testimony or in schedules when the duty arose. The court finds these sufficiently connected to allow relation back (and thus timely) assertion of the theories set forth in the amended complaint. Surely the law cannot be that a plaintiff is kept from introducing more recently-discovered further examples of the same sort of offense as described in the original complaint.

Even less persuasive is the defendant's second basis for the motion. Here, defendant, citing the *Twombly* and *Iqbal* cases and Rule 9, argues that the amended complaint still does not contain sufficient detail allowing reasonable formation of an answer. Actually, the amended complaint contains a considerable (and more than sufficient) quantity of factual detail. First, *Twombly* and *Iqbal,* properly understood, merely hold for the proposition that a complaint must contain sufficient allegations of fact so as to create a plausible basis for relief. That standard is easily surpassed here. Second, although Rule 9 requires a greater allegation of factual detail to support fraud, this does not mean that a complaint must contain every conceivable fact supporting the claim. For example, the court doubts that the plaintiff has to allege exactly what debtor received in exchange for his Maserati or what the alleged value of RSL was. This sort of detail will come out in discovery. Nor is it necessary that Mr. Maahs and

Ms. Vallefuco fit within the statutory definition of "insiders" found at § 101(31). "Insiders" can be as expressed in common parlance in this context. The purpose in the federal pleading system is to give adequate notice of what must be defended, with sufficient detail to raise theories of liability beyond a speculative level. The rest is properly dealt with during the course of the litigation.

***3** The Defendant's motion to dismiss is DENIED.

The Defendant shall file an answer to Plaintiff's first amended complaint within thirty (30) days of entry of this order.

**All Citations**

Not Reported in B.R. Rptr., 2014 WL 12665719

# PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is: 2029 Century Park East, Suite 3100, Los Angeles, CA 90067

A true and correct copy of the foregoing document entitled (*specify*): **REPLY OF DEFENDANT, UMB BANK, IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT** will be served or was served **(a)** on the judge in chambers in the form and manner required by LBR 5005-2(d); and **(b)** in the manner stated below:

**1**. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**: Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On (*date*) October 24, 2019, I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

- Alexandra Achamallah aachamallah@milbank.com, rliubicic@milbank.com
- Nicholas A Koffroth nick.koffroth@dentons.com, chris.omeara@dentons.com
- Samuel R Maizel samuel.maizel@dentons.com, alicia.aguilar@dentons.com;docket.general.lit.LOS@dentons.com;tania.moyron@dentons.com;kathryn.howard@dentons.com;joan.mack@dentons.com;derry.kalve@dentons.com
- Tania M Moyron tania.moyron@dentons.com, chris.omeara@dentons.com;nick.koffroth@dentons.com
- Abigail V O'Brient avobrient@mintz.com, docketing@mintz.com;DEHashimoto@mintz.com;nleali@mintz.com;ABLevin@mintz.com;GJLeon@mintz.com
- Mark Shinderman mshinderman@milbank.com, dmuhrez@milbank.com;dlbatie@milbank.com
- United States Trustee (LA) ustpregion16.la.ecf@usdoj.gov

☐ Service information continued on attached page

**2. SERVED BY UNITED STATES MAIL**:
On (*date*) _____, I served the following persons and/or entities at the last known addresses in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

☐ Service information continued on attached page

**3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL** (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on (*date*) October 24, 2019, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

VIA FEDERAL EXPRESS
Honorable Ernest Robles
U.S. Bankruptcy Court
Roybal Federal Building
255 E. Temple Street, Suite 1560
Los Angeles, CA 90012

☐ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

| | | | |
|---|---|---|---|
| 10/24/19 | Diane Hashimoto | | /s/ Diane Hashimoto |
| *Date* | *Printed Name* | | *Signature* |

# EXHIBIT B

Jason D. Strabo (SBN 246426)
McDermott Will & Emery LLP
2049 Century Park East, Suite 3200
Los Angeles, CA 90067-3206
Telephone: 310.788.4125
Facsimile: 310.277.4730
Email: jstrabo@mwe.com

Nathan F. Coco (admitted pro hac vice)
Megan Preusker (admitted pro hac vice)
McDermott Will & Emery LLP
444 West Lake Street, Suite 4000
Chicago, IL 60606-0029
Telephone: 312.372.2000
Facsimile: 312.984.7700
Email: ncoco@mwe.com
mpreusker@mwe.com

Clark T. Whitmore (admitted pro hac vice)
Jason M. Reed (admitted pro hac vice)
Maslon LLP
90 S. 7th Street, Suite 3300
Minneapolis, MN 55402
Telephone: 612.672.8200
Facsimile: 612.642.8301
Email: clark.whitmore@maslon.com
jason.reed@maslon.com

*Attorneys for U.S. Bank National Association, not individually but as Notes Trustee*

**UNITED STATES BANKRUPTCY COURT**
**CENTRAL DISTRICT OF CALIFORNIA**
**LOS ANGELES DIVISION**

| | |
|---|---|
| In re:<br><br>VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*,<br><br>Debtors. | Lead Case No. 2:18-bk-20151-ER<br><br>Chapter 11<br><br>Adv. Proc. No. 2:19-ap-01165-ER |
| OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*,<br><br>Plaintiff,<br><br>v.<br><br>U.S. BANK NATIONAL ASSOCIATION, as Trustee,<br><br>Defendant. | **MOTION OF U.S. BANK NATIONAL ASSOCIATION, AS NOTES TRUSTEE TO DISMISS AMENDED COMPLAINT; MEMORANDUM IN SUPPORT THEREOF**<br><br>Date: November 21, 2019<br>Time: 10:00 am<br>Judge: Hon. Ernest M. Robles<br>Place: U.S. Bankruptcy Court<br>Courtroom 1568<br>Edward R. Roybal Federal Building<br>255 East Temple Street<br>Los Angeles, CA 90012 |

**TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:**

**PLEASE TAKE NOTICE THAT** on November 21, 2019, at 10:00 a.m., or as soon thereafter as the matter may be heard, before the Honorable Judge Ernest M. Robles of the United States Bankruptcy Court for the Central District of California, located in Courtroom 1568, of the above-entitled Court, located at 255 East Temple Street, Los Angeles, CA 90012 Defendant U.S. Bank National Association in its respective capacities as Series 2015 Note Trustee and as Series 2017 Note Trustee (together, the "**Notes Trustee**"), will and hereby does move (this "**Motion**") pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure, which is applicable to this Adversary Proceeding under Rule 7012 of the Federal Rules of Bankruptcy Procedure, for entry of an order dismissing the First Amended Complaint for Determination of Validity, Priority, and Extent of Lien and Security Interests [Dkt. No. 30] (the "**Amended Complaint**") filed by Plaintiff Official Committee of Unsecured Creditors (the "**Committee**") for the reasons stated herein.

Under LBR 9013-1(f) any written response is to be filed and served at least fourteen days before the hearing, but per the stipulation among the parties, Plaintiff's response is to be filed and served by October 17, 2019 and Defendants' reply is to be filed and served by October 24, 2019.

This Motion is supported by the Memorandum of Points and Authorities in Support included herein, and the filed pleadings, documents or facts in the Debtors' chapter 11 bankruptcy cases for which Court may take judicial notice, applicable legal authority, and the arguments of counsel in support of this Motion.

Dated: September 30, 2019

**MCDERMOTT WILL & EMERY LLP**

By: /s/ *Jason D. Strabo*
Jason D. Strabo

**MASLON LLP**

By: /s/ *Clark T. Whitmore*
Clark T. Whitmore

*Attorneys for U.S. Bank National Association, not individually but as Notes Trustee*

**TABLE OF CONTENTS**

**Page**

## TABLE OF AUTHORITIES

**Page(s)**

**Cases**

**Statutes**



**Rules**

**MEMORANDUM OF POINTS AND AUTHORITIES**

The Committee's Amended Complaint,[1] brought in reliance upon the Challenge rights set forth the Final DIP Order (defined below), seeks a patchwork of judicial declarations against the Notes Trustee (as defined below) having no clear relevancy to the treatment of the Notes Trustee in the Debtors' proposed Plan of Liquidation. On the other hand, all of the issues raised in the Amended Complaint would be rendered moot by the confirmation of the Debtors' Plan.[2] The Debtors (whose proposed Plan treats the Notes Trustee as fully secured) have requested that this Court schedule a hearing on confirmation of the Plan on November 21, 2019, and it is supported by all of the Prepetition Secured Creditors, including the Notes Trustee. By the time of the confirmation hearing, the currently pending sale of the Debtors' remaining Hospitals to Strategic Global Management, Inc. ("**SGM**") is expected to have closed, providing a key source of funding for the Plan. At the hearing on confirmation, the Notes Trustee (alongside the Debtors and other Prepetition Secured Creditors) will present evidence that the prepetition and postpetition replacement liens of the Notes Trustee (whose liens are first in priority) and superpriority administrative expense claims support payment of the Notes as provided by the Plan.

The proposed Plan is the culmination of more than a year's worth of work by the Debtors, supported by the Prepetition Secured Creditors, including the Notes Trustee, which has centered on maintaining the Debtors as a going concern to maximize value for the Debtors' estates. Maintaining operations and selling the Debtors' assets as a going concern (even as significant ongoing financial losses have continued to mount), rather than shutting the facilities down, has benefitted the Debtors' general unsecured creditors who should receive a substantial distribution under the Plan, assuming that administrative expenses, such as litigation costs, can be appropriately limited.

Keeping the Hospitals operational during these cases was possible in part because the Debtors' Prepetition Secured Creditors, including the Notes Trustee, (a) permitted their perfected prepetition liens to be primed by a $185 million DIP facility, and (b) consented to the use of

[1] The First Amended Complaint for Determination of Validity, Priority, and Extent of Lien and Security Interests [Dkt. No. 30] (19-ap-1165) filed September 11, 2019 shall be referred to as the "**Amended Complaint**".

[2] The Debtors' Chapter 11 Plan of Liquidation (Dated September 3, 2019), [Dkt. No. 2993] shall be referred to as the "**Plan**".

hundreds of millions of dollars of their cash collateral throughout the course of the bankruptcy cases to fund operating losses and pay administrative expenses. As part of this undertaking, the Debtors proposed a number of protections and stipulations, as well as adequate protection for Prepetition Secured Creditors that were included after an interim and final hearing in the Court's *Final Order (I) Authorizing Postpetition Financing, (II) Authorizing Use of Cash Collateral, (III) Granting Liens and Providing Superpriority Administrative Expense Status, (IV) Granting Adequate Protection, (V) Modifying Automatic Stay, and (VI) Granting Related Relief (the "**Final DIP Order**")* [Dkt. No. 409].[3] In the Final DIP Order the Court found that the Prepetition Creditors were oversecured and together held liens upon substantially all of the assets of the Debtors as of the Petition Date.

The Final DIP Order granted the Committee limited standing within a designated Challenge Period without further leave of Court to challenge the Prepetition Liens (as defined in the Final DIP Order) of the Notes Trustee in the property of the Debtors as of the Petition Date. The Committee has never disputed the amount of the Notes Trustee's claim and, in December 2018, pursuant to a stipulation entered into between the Notes Trustee and the Committee, the Committee affirmatively waived its right to challenge the validity and enforceability of the Notes Trustee's prepetition liens on all of the present and after acquired collateral of the Notes Trustee described in its expansive loan documents, including substantially all rights to payment, except for certain bank accounts which allegedly lacked deposit control agreements in favor of the Notes Trustee. The Amended Complaint seeks a declaration that any funds in these accounts as of the Petition Date were not subject to the Notes Trustee's liens due to the alleged lack of deposit control agreements even though the funds in question were almost certainly the identifiable cash proceeds of other Notes Trustee liens and the money no longer exists.

The other claims in the Amended Complaint extend beyond the Committee's standing as provided in the Final DIP Order to seek judicial declarations that do not pertain to the Prepetition Liens as of the Petition Date, fail to present a present case or controversy, ignore the overriding rights granted by this Court to the Notes Trustee in the Final DIP Order and by the Committee's own

[3] Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to them in the Final DIP Order and the Supplemental Cash Collateral Order (defined herein).

stipulated waivers, or are simply contrary to applicable law. Accordingly, each of the claims set forth in the Amended Complaint should be dismissed at this time.

The Amended Complaint is, at its core, a disguised partial objection to the Notes Trustee's treatment under the proposed Plan, and the substance of all such objections can and should be addressed at the confirmation hearing when the Court will have a complete record, including an understanding of the Prepetition Secured Creditors' postpetition replacement liens and superpriority administrative expense claims that are not addressed in the Amended Complaint.

## FACTUAL BACKGROUND

1. Defendant U.S. Bank National Association serves as indenture trustee and collateral agent (in such capacities, the "**Notes Trustee**) for the holders of $202,000,000 in outstanding principal amount of Notes issued in 2015 and 2017 (collectively, the "**Notes**") by the California Public Finance Authority as a public finance conduit for Verity Health System of California, Inc. ("**VHS**") and its Obligated Members consisting of the St. Francis Medical Center, St. Vincent Medical Center, O'Connor Hospital, Saint Louise Regional Hospital, and Seton Medical Center, including Seton Medical Center Coastside (each, a "**Hospital Debtor**" and collectively, the "**Hospital Debtors**"). Of the $202,000,000 in principal amount of Notes, $160,000,000 was issued in four series pursuant to individual Indentures each dated as of December 1, 2015. The remaining $42,000,000 of Notes were issued in two series pursuant to two Indentures dated as of September 1, 2017 and December 1, 2017, respectively.

2. The proceeds of each series of Notes were loaned to VHS and the Hospital Debtors pursuant to corresponding Loan Agreements dated as of December 1, 2015, with respect to the 2015 Notes, and Loan Agreements dated as of September 1, 2017 and December 1, 2017, with respect to the 2017 Notes, each between the Authority and VHS, for itself and the Hospital Debtors.

3. The Loan Agreement for each series of Notes is accompanied by six substantially identical Security Agreements (as amended, the "**Security Agreements**") executed by VHS and each Hospital Debtor, respectively, in favor of the Notes Trustee on the same date as the corresponding Loan Agreement to which it relates.[4] Each of the Security Agreements was amended and restated

[4] Copies of the Security Agreements were filed in the Debtors' bankruptcy cases at Dkt. No. 367-1.

most recently on December 1, 2017, pursuant to which VHS and each Hospital Debtor granted the Notes Trustee a:

> continuing, first priority security interest in, all of Hospital Debtor's right, title, and interest in and to the following property of such Hospital Debtor, in each case whether now or hereafter existing or in which Hospital Debtor now has or hereafter acquires an interest and wherever the same may be located:
>
> (a) All Accounts;
>
> (b) Certain bank accounts (the "**Bank Accounts**") and all amounts deposited therein that are subject to Deposit Account Control Agreements, including, without limitation, those Bank Accounts listed on Schedule II annexed hereto[5]; and
>
> (c) All products, Proceeds and replacements thereof.

Security Agreement, § 2 (collectively, the "**Security Agreement Collateral**").

4. Each underlying Security Agreement defines "Accounts" broadly to capture all forms of revenue and rights of payment:

> "Accounts" means collectively, (a) any right to payment of a monetary obligation whether or not earned by performance, that relates to or arises out of any services provided or goods rendered by an Obligated Group Member (including, without limitation, payments made by or through a governmental authority to an individual patient assigned to such Member), (b) without duplication, any 'account' (as defined in the UCC), any accounts receivable, whether in the form of payments for services rendered or goods sold, rents, license fees or otherwise), any Health-Care-Insurance Receivables (as defined in the UCC) and any Payment Intangibles (as defined in the UCC), (c) all General Intangibles (as defined in the UCC), Intellectual Property (as defined in the UCC), rights, remedies, guarantees, supporting obligations and letter of credit rights relating to or arising out of the foregoing assets described in clauses (a) and (b), (d) all information and data compiled or derived by any Member or to which any Member is entitled in respect of or related to the foregoing assets described in clauses (a) and (b) and (e) and all proceeds of any of the foregoing.

Security Agreement, Schedule V.

5. To perfect its security interest in the Security Agreement Collateral, the Notes Trustee filed Uniform Commercial Code ("**UCC**") Financing Statements, and appropriate amendments with the California Secretary of State. The UCC Financing Statements each perfected the Security Agreement Collateral against VHS and each of the relevant Hospital Debtors in all "Accounts" and "[a]ll products, Proceeds and replacements thereof." *Id.*

[5] These bank accounts include the 34 accounts of the Hospital Debtors referenced in Count II of the Amended Complaint.

6. The Notes are further secured by (a) that certain Deed of Trust with Fixture Filing and Security Agreement and Assignment of Leases and Rents by Saint Louise Regional Hospital dated December 14, 2015 (as amended and restated September 1, 2017, and further amended and restated December 1, 2017); (b) those certain Deeds of Trust with Fixture Filing and Security Agreement and Assignment of Leases and Rents by St. Francis Medical Center dated December 14, 2015 (as each was amended and restated September 1, 2017, and further amended and restated December 1, 2017).[6]

7. The indebtedness evidenced by the 2017 Notes is additionally secured by a Deed of Trust with Fixture Filing and Security Agreement and Assignment of Rents and Leases, dated September 15, 2017, as amended (the "**Moss Deed of Trust**"), granted by Verity Holdings LLC on certain real estate and related property located in San Mateo County, California (the "**Moss Property**").

8. The Notes are also entitled to share on a *pro rata* basis with the other Obligations under the Master Indenture, including the Series 2005 Bonds,[7] the benefits of the collateral pledged under the Master Indenture. Those Obligations are secured by, *inter alia*, (i) Deeds of Trust on each of the Hospital Debtors, and (ii) the "Gross Revenues" of VHS and the Hospital Debtors, which is broadly defined to include "all revenues, income, receipts and money received by or on behalf of the Members from all sources".

9. Pursuant to that certain Intercreditor Agreement dated as of December 1, 2015, as amended by the Amended and Restated Intercreditor Agreement dated as of September 1, 2017, as further amended by the Second Amended and Restated Intercreditor Agreement dated as of December 1, 2017 (as amended, the "**Intercreditor Agreement**"), the Master Trustee subordinated its liens and security interests, including the Gross Revenue pledge, to the Notes Trustee with respect to the Senior Note Collateral as described therein.[8] As a result, the Notes Trustee held, among other

[6] Copies of the Deeds of Trust were filed in the Debtors' bankruptcy cases at Dkt. No. 367-1.

[7] In addition to the Notes, the Obligations under the Master Indenture also include the California Statewide Communities Development Authority Revenue Bonds (Daughters of Charity Health System) Series 2005A, F, G and H (the "**Series 2005 Bonds**").

[8] A copy of the Intercreditor Agreement was filed in the Debtors' bankruptcy cases at Dkt. No. 367-1.

things, first priority, perfected liens in all of the working capital assets of VHS and each of the Hospital Debtors and first priority deeds of trust covering the two most valuable Hospitals, St. Francis and Saint Louise.

10. On August 31, 2018 (the "**Petition Date**"), the Debtors each filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code, commencing the above-captioned chapter 11 cases.

11. On the Petition Date, the Debtors also filed the *Emergency Motion of Debtors for Interim and Final Orders (A) Authorizing the Debtors to Obtain Post Petition Financing, (B) Authorizing the Debtors to Use Cash Collateral, and (C) Granting Adequate Protection to Prepetition Secured Creditors Pursuant to 11 U.S.C. §§ 105, 363, 364, 1107 and 1108; Memorandum of Points and Authorities in Support Thereof* [Dkt. No. 31] (the "**DIP Motion**"). The DIP Motion sought approval of postpetition financing in an amount up to $185 million, secured by a lien on substantially all the Debtors' present and future assets.

12. In connection with the DIP Motion, the Notes Trustee negotiated to provide its consent to being primed by the DIP Loans and to the use of the cash collateral of the Hospital Debtors to fund continuing operations during a consensual process to sell the hospital assets of the Debtors as going concerns. The DIP Lender refused to provide the DIP Loan without the consent of the Prepetition Secured Creditors, including the Notes Trustee. The Debtors agreed that the Notes Trustee (along with the other Prepetition Secured Creditors) was oversecured and asked the Court to provide the Notes Trustee with various forms of adequate protection, including Prepetition Replacement Liens, to protect it from the diminution in the value of its interests in prepetition collateral as of the Petition Date.

13. On October 3, 2018, this Court issued its tentative rulings regarding the DIP Motion [Dkt. No. 392] (the "**Tentative Ruling**"), which were expressly incorporated in and made a part of the Final DIP Order. The Court found that the Prepetition Secured Creditors held liens upon and security interests in substantially all the Debtors' assets, and that the secured creditors were oversecured with an equity cushion of between $150 and $200 million. Tentative Ruling p. 8. Specifically, the Court found that the Prepetition Secured Creditors, including the Notes Trustee, held

aggregate claims against the Debtors of approximately $565 million, and that the Debtors' assets with proper marketing would be worth between $725 and $800 million. *Id.*

14. The Court found in the Final DIP Order that the Prepetition Secured Creditors were adequately protected and held that ". . . the equity cushion, the replacement liens and Superpriority claims provide the secured creditors additional adequate protection. The financing by the DIP Lender will enable the Debtors to continue to operate and generate additional receivables. Those receivables will be subject to the replacement liens." [Tentative Ruling pgs. 10-11].

15. On October 4, 2018, this Court entered the Final DIP Order, pursuant to which the Debtors acknowledged, and the Court found, that the Notes Trustee's lien in the Prepetition Secured Collateral is valid, binding, enforceable, non-avoidable, and properly perfected. The Final DIP Order also expressly incorporated each of the findings in the Tentative Rulings.

16. Specifically, Section 5(a) of the Final DIP Order states that, "[a]s adequate for the interests of the Prepetition Secured Creditors in the Prepetition Collateral … on account of the granting of the DIP Liens, subordination to the Carve Out …, any Diminution in Value arising out of the Debtors' use, sale, or disposition or other depreciation of the Prepetition Collateral, including Cash Collateral …, resulting from the automatic stay, the Prepetition Secured Creditors … shall receive adequate protection" in the form of "additional valid, perfected and enforceable replacement security interests and Liens in the DIP Collateral … ." Final DIP Order, ¶ 5(a). The Final DIP Order also granted the Notes Trustee and other Prepetition Secured Creditors a Prepetition Superpriority Claim to the extent of any diminution in the value of its interest in Prepetition Collateral. Final DIP Order, ¶ 5(d).

17. Additionally, because the Notes Trustee consented to having its Prepetition Liens primed by the DIP Lender, the Final DIP Order further waived the "equities of the case" exception under section 552(b) and trustee surcharge rights under section 506(c) of the Bankruptcy Code. "In light of the Prepetition Secured Creditors' . . . agreements that their Prepetition Liens . . . shall be subject to the Carve Out and subordinate to the DIP Liens, the Prepetition Secured Creditors . . . are each entitled to a waiver of any "equities of the case" exception under section 552(b) of the

Bankruptcy Code, and a waiver of the provisions of section 506(c) of the Bankruptcy Code. Final DIP Order, ¶ 5(f).

18. Section 5(e) of the Final DIP Order established a deadline for the Committee to challenge the Note Trustee's Prepetition Liens. It states that:

> The findings and stipulations set forth in this Final Order with respect to the validity, enforceability and amount of the Prepetition Secured Obligation and the Prepetition Liens shall be binding on any subsequent trustee, responsible person, examiner with expanded powers, any other estate representative, and all creditors and parties in interest and all of their successors in interest and assigns, including the Committee, unless, and solely to the extent that, a party in interest with requisite standing and authority (other than the Debtors, as to which any Challenge (as defined below) is irrevocably waived and relinquished) has timely filed the appropriate pleadings, and timely commenced the appropriate proceeding required under the Bankruptcy Code and Bankruptcy Rules, including as required pursuant to Part VII of the Bankruptcy Rules (in each case subject to the limitations set forth in this paragraph 4(d)) challenging the Prepetition Liens (each such proceeding or appropriate pleading commencing a proceeding or other contested matter, a "**Challenge**") within ninety (90) days from the formation of the Committee (the "**Challenge Deadline**"); provided that for purposes of filing a Challenge, the Committee shall be deemed to have standing to file the requisite pleading without further order of the Court; and *provided further*, that the "Challenge Deadline" for matters solely relating to the value of the Prepetition Collateral may be further extended to such time as may be agreed by stipulation among the Debtors, the Committee and the Prepetition Secured Creditors or as further ordered by the Court.

Final DIP Order, ¶ 5(e)

19. On December 13, 2018, the Committee and the Notes Trustee entered into a *Stipulation between U.S. Bank National Association and the Official Committee of Unsecured Creditors Extending Challenge Deadline* (the "**Challenge Stipulation**") [Dkt. No. 1048]. Pursuant to the Challenge Stipulation, the Committee agreed that "[i]n consideration of the extension of the Challenge Deadline for certain assets of the Debtors as provided herein below, the Committee acknowledges that *the Challenge Deadline shall not be extended for the Acknowledged Collateral*." Challenge Stipulation, p. 2 (emphasis added).

20. The definition of Acknowledged Collateral in the Challenge Stipulation includes:

> (1) perfected deed of trust liens and security interest in the real property (including Facilities and Appurtenances, Leases, Rents and Equipment to the extent they constitute real property) set forth on Exhibit A hereto (the deeds of trust to which such security interest relate being referred to herein as "**Mortgages**");
>
> (2) to the extent not covered by subparagraph (1) above, perfected deed of trust liens and security interests in the Facilities, Appurtenances, Equipment, Leases, Rents, Proceeds and Inventory of St. Francis Medical Center, Saint Louise Regional Hospital and Verity Holdings LLC, in each case to the extent such property is (i) described in the corresponding financing

statements filed with the California Secretary of State and (ii) can be perfected by the filing of a financing statement with the California Secretary of State. Any capitalized terms used in this paragraph which are not otherwise defined herein shall have the meaning assigned to such terms in the applicable Mortgages;

(3) a perfected security interest in the following personal property of Seton Medical Center, Seton Coastside, Saint Louise Regional Hospital, St. Francis Medical Center, O'Connor Hospital and St. Vincent Medical Center:

(a) Accounts (as defined in the Security Agreements referred to in the Loan Agreements); and

(b) All products, replacements and Proceeds (as defined in the California Uniform Commercial Code) of the property described in the preceding clause (a).

*Id*. at 3.

21. The Challenge Stipulation incorporated by reference the definition of "Accounts" set forth in the Security Agreements described in paragraph 4 above, which includes, *inter alia*, (i) any "right to payment of a monetary obligation whether or not earned by performance, that relates to or arises out of any services provided or goods rendered by an Obligated Group Member (including, without limitation, payments made by or through a governmental authority to an individual patient assigned to such Member)," (ii) any "account" as defined in the UCC, (iii) any "accounts receivable, whether in the form of payments for services rendered or goods sold, rents, license fees or otherwise, Health-Care-Insurance Receivables (as defined in the UCC)," and (iv) any "Payment Intangibles" and "General Intangibles" (each as defined in the UCC).

22. The fact that the Committee waived its challenge rights with respect to "Accounts" (*i.e*., "Acknowledged Collateral") under the Challenge Stipulation is significant because the Notes Trustee would not have otherwise agreed to extend the investigation period for the Committee under the Final DIP Order. Through the definition of "Acknowledged Collateral" set forth in the Challenge Stipulation, which expressly includes the term "Accounts" as defined under the Security Agreements, the Committee forever and irrevocably waived its right to later challenge the validity and perfection of the Notes Trustee's security interest in said "Accounts":

> The Committee has delivered correspondence to the Trustee *acknowledging the Trustee's valid and perfected security interest in some but not all of the assets of the Debtors as set forth in paragraph A below (the "Acknowledged Collateral")*. The Trustee and the Committee are discussing the extent and priority of liens with respect to that portion of the Debtors' assets not included within the Acknowledged Collateral.

Challenge Stipulation, ¶ 5 (emphasis added).

23. The rights of the Hospital Debtors to receive payments for care and services provided to patients of the Hospital Debtors of any type, including delayed QAF distributions from the California Department of Health Services, are "Accounts" of the Hospital Debtors and/or "proceeds" of Accounts within the definition of Acknowledged Collateral as set forth in the Security Agreements and the Challenge Stipulation.

24. The Challenge Deadline was extended five additional times by the Notes Trustee and the Committee with respect to challenges and liens *other than Acknowledged Collateral* on January 14, 2019 [Dkt. No. 1251], February 15, 2019 [Dkt. No. 1560], March 15, 2019 [Dkt. No. 1824], May 13, 2019 [Dkt. No. 2366], and May 31, 2019 [Dkt. No. 2480]. None of the additional extensions modified the rights of either the Notes Trustee or the Committee beyond extending the challenge period for the collateral rights not previously conceded by the Committee.

25. In June of 2019, before the final Challenge Deadline on June 13, 2019, the Committee filed its original adversary Complaint for Determination of Validity, Priority, and Extent of Liens and Security Interests (Docket No. 1, the "**Original Complaint**"). The initial Complaint sought: (a) to modify language in the Final DIP Order; (b) declarations that the Notes Trustee did not have a perfected security interest in an unspecified amount of cash held by the Debtors as of the Petition Date in certain bank accounts; and (c) declarations that Future QAF Disbursements not yet paid to the Hospital Debtors relating to post petition services and "commercial tort claims" would not be subject to the perfected security interests of the Notes Trustee.

26. On December 27, 2018, the Committee appealed from the Final DIP Order, solely with respect to the waivers of the "equities of the case" exception to Section 552(b) and the trustee surcharge rights under Section 506(c) of the Bankruptcy Code. That appeal was dismissed by the district court as moot on August 2, 2019, and the Committee has further appealed that dismissal to the Ninth Circuit Court of Appeals, where it remains pending at this time.

27. The Committee's appeals of the Final DIP Order have not included any appeal of the Court's ruling regarding the oversecured status of the Prepetition Secured Creditors or the Court's grant of adequate protection including Prepetition Replacement Liens and related superpriority claims

to the extent of any "diminution in value" of the interests of the Notes Trustee in the property of VHS and the Hospital Debtors. Nor did the Committee's appeal of the Final DIP Order include any appeal of the scope or effect of the lien challenge provision thereof.

28. In its brief to the District Court on appeal, the Committee, in fact, affirmatively relied upon this Court's determination in the Final DIP Order of a substantial equity cushion in favor of the Prepetition Secured Creditors as of the Petition Date to argue for the elimination of provisions in the Final DIP Order for a waiver of the "equities of the case" exception to Section 552(b) and the Trustee's right of surcharge in Section 506(c) of the Bankruptcy Code. *See* Case No. 2:18-cv-10675(RGK), Docket No. 22, pp. 19, 27 & 32 (noting that "the Bankruptcy Court had found [the Prepetition Secured Creditors] were already fully protected by an equity cushion in excess of 25%," and that "the claims of the Prepetition Secured Creditors were significantly oversecured").

29. On September 11, 2019, the Committee filed its Amended Complaint. The Amended Complaint adds allegations that the Notes Trustee does not have a security interest in certain "MOB Assets" and the so-called "going concern premium" obtained for any collateral sold, or to be sold, during the bankruptcy cases. The Amended Complaint alleges conditionally—for the first time—that if Future QAF Disbursements are determined to be proceeds of the Security Agreement Collateral as a result of modifications to a loan agreement, such modifications should be avoided under the California Fraudulent Transfers Act. Finally, the Amended Complaint includes a new count seeking a declaration that the Notes Trustee would be undersecured if the Court were to grant the other declarations being sought.

**LEGAL STANDARD**

"[A] motion to dismiss under Federal Rule of Civil Procedure 12(b)(6) asserts that the complaint fails to state a claim upon which relief may be granted. Dismissal may be based on either 'the lack of a cognizable legal theory or the absence of sufficient facts alleged under a cognizable legal theory.'" *Balistreri v. Pacifica Police Dep't*, 901 F.2d 696, 699 (9th Cir. 1990). For purposes of evaluating a motion to dismiss, a court "must presume all factual allegations of the complaint to be true and draw all reasonable inferences in favor of the nonmoving party." *Usher v. City of L.A.*, 828 F.2d 556, 561 (9th Cir. 1987). A complaint must plead "enough facts to state a claim to relief

that is plausible on its face." *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570, 127 S. Ct. 1955, 167 L.Ed.2d 929 (2007). "A claim is plausible 'when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.'" *Landmark Am. Ins. Co. v. Navigators Ins. Co.*, 354 F. Supp. 3d 1078, 1081–82 (N.D. Cal. 2018) (*quoting Ashcroft v. Iqbal*, 556 U.S. 662, 678, 129 S. Ct. 1937, 173 L.Ed.2d 868 (2009)). It is axiomatic that a claim cannot be plausible when it has no legal basis. Therefore, a dismissal under Federal Rule 12(b)(6) may be based either on the lack of a cognizable legal theory or on the absence of sufficient facts alleged under a cognizable legal theory. *See Johnson v. Riverside Healthcare Sys, LP*, 534 F.3d 1116, 1121 (9th Cir. 2008).

"Threadbare recitals of the elements of a cause of action, supported by mere conclusory statements, do not suffice" to state a cognizable claim. *Iqbal*, 556 U.S. at 678. And "the tenet that a court must accept as true all of the allegations contained in a complaint is inapplicable to legal conclusions." *Id*. Accordingly, "where the well-pleaded facts do not permit the court to infer more than the mere possibility of misconduct, the complaint has alleged—but it has not shown—that the pleader is entitled to relief." *Id*. at 679 (internal quotation marks omitted); *see Adams v. Johnson*, 355 F.3d 1179, 1183 (9th Cir. 2004). And "'a plaintiff may plead [him]self out of court'" if he "plead[s] facts which establish that he cannot prevail on his . . . claim." *Weisbuch v. County of Los Angeles*, 119 F.3d 778, 783 n.1 (9th Cir. 1997) (quoting *Warzon v. Drew*, 60 F.3d 1234, 1239 (7th Cir. 1995)).

## ARGUMENT

### I. THE COMMITTEE LACKS STANDING TO BRING CHALLENGES BEYOND THE SCOPE OF THE ENUMERATED CHALLENGES IDENTIFIED IN SECTION 5(E) OF THE FINAL DIP ORDER.

The Amended Complaint purports to be based entirely upon the Challenge standing conferred by the Court in Section 5(e) of the Final DIP Order, but the Committee's claims go far beyond it. Counts I, III and IV of the Amended Complaint should be dismissed because they are beyond the scope of the enumerated challenges identified in section 5(e) of the Final DIP Order. Section 5(e) does not contemplate claims or causes of action related to postpetition matters, such as the rights of parties with respect to postpetition Future QAF Payments or the proper method for the

Court to use in determining the value of the Notes Trustee's rights in existing and future postpetition Hospital sales proceeds characterized by the Committee as a "going concern premium."[9]

The Committee's claims and challenges (which now include a newly-added fraudulent transfer claim) go beyond the scope of the limited standing conferred under section 5(e) of the Final DIP Order. The Debtors are the representatives of the bankruptcy estates, and the Committee's powers and standing in these bankruptcy cases are limited by Section 1103 of the Bankruptcy Code, which does not authorize lawsuits against creditors on behalf of the bankruptcy estate without leave of court. Before exceeding the Court's sanctioned standing under the Final DIP Order ,the Committee was required to bring a motion for leave and demonstrate, *inter alia*, that (1) the claims it seeks to bring are colorable, and (2) the Debtors have unjustifiably refused to pursue such claims. *See In re Yes! Entertainment Corp*., 316 B.R. 141, 145 (D. Del. 2004). *See also Official Comm. Of Unsecured Creditors of Sunbeam Corp. v. Morgan Stanley & Co*. (In re Sunbeam Corp.), 284 B.R. 355, 375 (Bankr. S.D.N.Y. 2002) (denying standing to committee where failed to demonstrate that prosecution of the actions would be "necessary and beneficial" to the resolution of the bankruptcy proceedings).

Pursuant to Section 5(e) of the Final DIP Order, the findings and stipulations set forth in the Final DIP Order with respect to the Prepetition Secured Obligations and the Prepetition Liens are binding on the bankruptcy estates and its creditors unless and solely to the extent that a party in interest has filed a timely Challenge by appropriate proceedings within the designated 90-day period, with an initial deadline of December 13, 2018. The Committee was thus granted standing to file an appropriate Challenge, but subject to the limitations set forth in Section 5(e) and the purposes for which standing was granted in the Final DIP Order.

However, Counts I, III and IV of the Amended Complaint go well beyond the Court-sanctioned Challenge of pre-petition liens and security interests; they seek relief with respect to property acquired by the Debtors' estates long after the Petition Date. The Debtors did not make any

[9] The Committee's novel request in Count I for a declaration that a "going concern premium" be deducted from the Notes Trustee's Prepetition Liens and collateral sale proceeds is manifestly contrary to both the Final DIP Order and binding precedent in the Ninth Circuit on the proper valuation of collateral sold as part of a going concern. *See*, *e.g.*, *In re Sunnyslope Housing L.P.*, 859 F.3d 637 (9th Cir. 2017).

stipulations in the Final DIP Order about the collateral value of postpetition assets or the outer limits of Section 552(b) of the Bankruptcy Code as applied to future assets and events. Yet, the Committee improperly seeks to expand its Challenge right to include relief regarding the attachment of Prepetition Liens to Future QAF Disbursements and a newly-imagined asset class referred to as the "going concern premium" of the Notes Trustee collateral sold with its consent. Count III also tacks onto its claim to Future QAF Disbursements an improper new contingent fraudulent conveyance claim regarding future assets with respect to unspecified loan agreement amendments. Amended Complaint, ¶ 36. None of these claims fall within the Court's narrowly-tailored grant of derivative standing under section 5(e) of the Final DIP Order. The Challenges permitted by the Final DIP Order were naturally intended only to enable a review of the status of the Notes Trustee's lien rights as of the Petition Date, not to cover whatever issues the Committee might conjure up on the eve of confirmation to block confirmation of the Debtors' proposed Plan. Any improper effort to obtain negotiating leverage by threatening to delay confirmation of a time-sensitive Plan should not be tolerated.

The Committee's new Count IV—seeking a conditional determination that the Notes Trustee is rendered undersecured— is a striking example of the kind of claim that cannot properly be brought pursuant to Section 5(e) of the Final DIP Order. Not only is it an improper collateral attack on the Court's prior finding that the Prepetition Secured Creditors are over-secured, but in order to adjudicate Count IV, the parties would be required to litigate – and the Court would be required to evaluate – the Notes Trustee's Prepetition Replacement Liens on postpetition assets, to the extent not otherwise subject to its Prepetition Liens.

Count III, dealing with Future QAF Disbursements, and Count IV both turn on the extent to which value accumulating to the Debtors' bankruptcy estates post-petition count as part of the Notes Trustee's secured claim for Plan treatment purposes.[10] These are not Challenges within the meaning of the Final DIP Order and should be dismissed.

[10] In 2017 Bankruptcy Rule 7001 (2) was clarified to provide that a proceeding to determine the secured amount of a creditors' claim should proceed by motion under Rule 3012 and not be adversary proceeding. To the extent that Count IV may be construed as a claim to determine the amount of the secured claim of the Notes Trustee for confirmation purposes, it should be brought under Rule 3012 by the appropriate party. The Amended Complaint is equivocal about whether Replacement Liens granted to the Notes Trustee are covered by Count IV.

## II. THE COMMITTEE'S LIEN CHALLENGE WITH RESPECT TO THE HOSPITAL DEBTORS' DEPOSIT ACCOUNTS WAS WAIVED AND IRRELEVANT, IN ANY EVENT.

### A. The Committee Has Waived the Right to Challenge Whether Proceeds Held in the Hospital Debtors' Deposit Accounts are the Proceeds of the Collateral of the Notes Trustee.

Count II of the Amended Complaint should be dismissed because the Committee waived its right to challenge the validity and perfection of the Notes Trustee's liens and security interests with respect to the proceeds of "Accounts" (as broadly defined) held in the Hospital Debtors' deposit accounts as of the Petition Date. As noted above, the initial Challenge deadline was December 13, 2018. That Challenge deadline was extended by the Notes Trustee in a Challenge Stipulation, but only with respect to assets not constituting Acknowledged Collateral. Under the Challenge Stipulation, any claim that could have been asserted against the Notes Trustee with respect to "Acknowledged Collateral," including "Accounts" as defined in the Security Agreements, is now time-barred under the deadlines established in the Final DIP Order.

Settlements and compromises are favored in bankruptcy as they minimize costly litigation and further parties' interests in expediting the administration of the bankruptcy estate. *Myers v. Martin (In re Martin)*, 91 F.3d 389, 393 (3d Cir. 1996); *In re Kerner*, 599 B.R. 751, 754 (Bankr. S.D.N.Y. 2019). The Ninth Circuit has stated that "stipulations serve both judicial economy and the convenience of the parties, courts will enforce them absent indications of involuntary or uninformed consent." *CDN Inc. v. Kapes*, 197 F.3d 1256, 1258 (9th Cir. 1999) (*citing United States v. McGregor*, 529 F.2d 928, 931 (9th Cir. 1976)). In fact, "[a] litigant can no more repudiate a compromise agreement than he could disown any other binding contractual relationship . . . . Moreover, it is equally well settled in the usual litigation context that courts have inherent power summarily to enforce a settlement agreement with respect to an action pending before it; the actual merits of the controversy become inconsequential . . . . The authority of a trial court to enter a judgment enforcing a settlement agreement has as its foundation the policy favoring the amicable adjustment of disputes and the concomitant avoidance of costly and time-consuming litigation." *Matter of Springpark Assocs.*, 623 F.2d 1377, 1380 (9th Cir. 1980) (superseded on other grounds by statute) (*quoting Dacanay v. Mendoza*, 573 F.2d 1075, 1078 (9th Cir. 1978)). The Ninth Circuit has

also found that "A bankruptcy court, as a court of equity, likewise possesses the power to summarily enforce settlements." *In re City Equities Anaheim, Ltd.*, 22 F.3d 954, 958 (9th Cir. 1994).

Count II identifies thirty-four (34) depository accounts held by the Hospital Debtors (together, the "**Deposit Accounts**"[11]) and seeks a declaration that (1) the Notes Trustee has no perfected liens in the Deposit Accounts because the Notes Trustee does not have possession or control of the Deposit Accounts,[12] and (2) none of the "funds in the Deposit Accounts constitute the identifiable cash proceeds of an otherwise perfected, unavoidable lien in other collateral of the Defendant."

While perfection in a deposit account itself generally requires control under UCC 9-314, the requirements for perfecting in identifiable cash proceeds only require the filing of a financing statement perfecting in the original collateral. See Cal. Com. Code § 9310(a). The Committee itself has acknowledged this. [Dkt. No. 3000; ¶ 2]. Except as otherwise provided in UCC sections 9310(b) and 9312(b), a financing statement must be filed to perfect all security interests and agricultural liens. Cal. Com. Code § 9310. Further, under California law, a secured creditor's lien attaches to the proceeds of its collateral notwithstanding a subsequent "sale, lease, license, exchange, or other disposition thereof … ." Cal. Com. Code § 9315.

There is no dispute that the Notes Trustee filed the requisite financing statements with the California Secretary of State covering the definition of Accounts and clearly identifying proceeds of such Accounts in the definition of its Prepetition Collateral. [See Exhibit B]. These financing statements cover all forms of payment to the Debtor Hospitals. The Amended Complaint does not and cannot allege to the contrary. Accordingly, Count II should be dismissed.

---

[11] The Amended Complaint includes fifteen other bank accounts within the definition of Deposit Accounts that are not with Debtors who are obligated to the Trustee. As discussed below, the Notes Trustee has not asserted a lien in deposit accounts not held by the Debtors obligated to it. There is no dispute as to these accounts and no reason to waste judicial resources seeking determinations with respect to such deposit accounts.

[12] Agreements governing and controlling several of these accounts among the Notes Trustee, Bank of America and the Debtors did exist. The Notes Trustee reserves all rights to assert that it did have control of these accounts by reason of these agreements, but the issue has little, if any, practical relevance because the funds therein would have been the identifiable proceeds of the liens of the Notes Trustee and, in any event, the funds have been spent by the Debtors and are not available.

In the Challenge Stipulation, the Committee irrevocably waived its right to make a Challenge of the security interests of the Notes Trustee in all of the Hospital Debtors' "Accounts," including

> (a) any right to payment of a monetary obligation whether or not earned by performance, that relates to or arises out of any services provided or goods rendered by an Obligated Group Member (including, without limitation, payments made by or through a governmental authority to an individual patient assigned to such Member), (b) without duplication, any 'account' (as defined in the UCC), any accounts receivable, whether in the form of payments for services rendered or goods sold, rents, license fees or otherwise), any Health-Care-Insurance Receivables (as defined in the UCC) and any Payment Intangibles (as defined in the UCC), (c) all General Intangibles (as defined in the UCC), Intellectual Property (as defined in the UCC), rights, remedies, guarantees, supporting obligations and letter of credit rights relating to or arising out of the foregoing assets described in clauses (a) and (b), (d) all information and data compiled or derived by any Member or to which any Member is entitled in respect of or related to the foregoing assets described in clauses (a) and (b) and (e) and all proceeds of any of the foregoing.

Security Agreement, Schedule V. As noted above, the definition of "Accounts" was broad and captured all forms of revenues and payments made to or collected by the Obligated Members. Accordingly, the Committee's waiver extends to all funds in the Deposit Accounts.

**B. <u>In Any Event, Count II Seeks Only an Irrelevant Judicial Declaration.</u>**

Count II fails to present a real case or controversy because the Committee fails to allege that any real money is at stake. The Court found in the Final DIP Order that the Prepetition Secured Creditors (which included the Notes Trustee) were oversecured as of the Petition Date and, therefore, are entitled to a Prepetition Replacement Lien in all DIP Collateral to the extent of any diminution. Moreover, the funds in the subject Deposit Accounts have been spent by the Debtors along with hundreds of millions of dollars of the Notes Trustee's other cash collateral. This fact begs the question—what difference would a judicial declaration about the status of liens in spent money as of the Petition Date make? If the money is gone, it cannot be divided or shared. For all the foregoing reasons, Count II should be dismissed.

**C. Count II Fails to Meet the Minimum Pleading Requirements for a Lien Challenge.**

Count II of the Amended Complaint should be dismissed because it fails to meet minimum pleading requirements. Count II hinges upon a blanket allegation that there are no "identifiable cash proceeds" in the Hospital Debtors' deposit accounts. Amended Complaint, ¶ 33. The allegation is

completely unquantified and unsubstantiated, and is in the nature of conclusory legal assertion. Given that the Notes Trustee has a perfected security interest in all forms of revenue and rights of payment, the allegation that none of the cash held by the Hospital Debtors as of the Petition Date constitutes the identifiable proceeds of the Notes Trustee's Prepetition Liens is incredulous.

"Pleadings must be something more than an ingenious academic exercise in the conceivable." *Jackson v. BellSouth Communications*, 372 F.3d 1250, 1271 (11th Cir. 2004). While it is perhaps conceivable that some of the funds in these Deposit Accounts are not subject to the liens of the Notes Trustee, the Committee must do more than it has done in the Complaint to support a claim. Complaints brought under the Bankruptcy Code are subject to the same pleading requirements as other complaints in federal court. *In re Tracht Gut, LLC*, 836 F.3d 1146 (9th Cir. 2016) (affirming dismissal of fraudulent transfer complaint for failure to state a claim when complaint merely repeated statutory elements and did not contain any factual allegations regarding why specific transfers might be fraudulent). A generalized claim for declaratory relief that does not contain a cognizable legal theory or factual basis supporting such theory is properly dismissed. *Id*. at 51.

The challenge right in the Final DIP Order was established to require the Committee to investigate claims and to assert challenges that it could support with enough specificity to meet the pleading requirements imposed upon plaintiffs generally. Because of the numerous extensions granted to it, the Committee had many months to determine what specific liens, if any, it would challenge. It also had ample time to develop factual predicates to plead enough facts to put the Notes Trustee on notice as to which funds, in which Deposit Accounts, the Committee believed were not subject to a security interest. The Committee's blunderbuss listing of dozens of potentially closed or empty Deposit Accounts and its demand for a declaration that none of these accounts contain funds that represent any identifiable cash proceeds of the Notes Trustee's collateral fails to meet the standards contemplated by the Final DIP Order, the Federal Rules of Civil Procedure and binding case precedent.

## III. THE NEW LIEN CHALLENGES ASSERTED BY THE COMMITTEE IN COUNTS I AND III OF ITS AMENDED COMPLAINT HAVE BEEN WAIVED.

The new lien challenges raised by the Committee for the first time in its Amended Complaint – *i.e.*, (i) the "going concern premium" challenge in Count I and (ii) the fraudulent conveyance challenge in Count III – were waived by the Committee and should be dismissed. As noted above, pursuant to stipulations entered into between the parties, the deadline for bringing lien Challenges under 5(e) of the Final DIP Order (even for collateral other than Acknowledged Collateral) expired on June 13, 2019. The Original Complaint did not include new claims asserted for the first time in the Amended Complaint. These include: (1) the new request in Count I for a declaration that the Court should not allow the Note Trustee to have Prepetition Liens upon "going concern premium" sales proceeds; (2) the new fraudulent conveyance allegation in Count III conditionally seeking to avoid any loan agreement amendments that may have captured a valid lien on Future QAF Disbursements and; (3) a new Count IV seeking a declaration that the Notes Trustee would be undersecured if the Court were to agree with the Committee's positions. As indicated above, these are not proper Challenges for which the Committee has standing, they have not been properly pled and have procedural defects. But, even if they were not otherwise subject to dismissal, and they are, these new claims have been raised too late, after the Challenge Deadline, and have therefore been waived.

Rule 15, is made applicable to this proceeding by Bankruptcy Rule 7015, does not save these new claims from being time barred. To relate back, that rule requires that "the claim or defense asserted in the amended pleading arose out of the conduct, transaction or occurrence set forth or attempted to be set forth in the original pleading…" *See* Fed. R. Civ. P. 15(c)(2). "[A]n amendment can only relate back if the new claim relies on the same facts and does not seek to insert new facts." *Id*. at 41. (reversing bankruptcy court's order granting leave to amend because untimely amended complaint pleaded new theory as well as new facts). The Ninth Circuit, in *Echlin v. PeaceHealth* held that:

> [C]laims must share a common core of operative facts such that the plaintiff will rely on the same evidence to prove each claim. Thus, an amendment will not

> relate back when the amended complaint had to include additional facts to support the new claim.

887 F.3d 967, 978 (9th Cir. 2018) (internal citations omitted).

Here, the facts alleged in the Original Complaint do not support the new claims asserted for the first time after the Challenge Deadline. *See* Amended Complaint, ¶¶ 22-24. Accordingly, these new claims, in addition to their other defects, have been waived as untimely.

## IV. THE COMMITTEE'S REQUESTS IN COUNT I TO RESTATE THE SCOPE OF THE PREPETITION LIENS OF THE NOTES TRUSTEE AND TO MODIFY THE FINAL DIP ORDER ARE IMPROPER.

In Count I of the Amended Complaint, the Committee seeks a declaration that, notwithstanding anything to the contrary in Section 5(e) of the Final DIP Order, the collateral of the Notes Trustee is limited as of the Petition Date to what the Committee describes as its collateral on Exhibit A to the Amended Complaint. This claim is an improper attempt to reformulate the waiver as to Acknowledged Collateral in the Challenge Stipulation. The Committee's Exhibit A does not fully describe the Acknowledged Collateral in the Challenge Stipulation in important respects. For example, it omits deposit accounts subject to deposit control agreements in favor of the Notes Trustee that are listed in the Acknowledged Collateral. Moreover, Exhibit A describes the collateral of the Notes Trustee in a truncated and abbreviated way that is more limited than the description of Acknowledged Collateral in the Challenge Stipulation or in the relevant underlying documentation. The substance of Count I is already covered by the Challenge Stipulation and cannot be varied and reformulated now.

To the extent that Count I is intended to clarify or modify Paragraph 5(e) of the Final DIP Order, it is procedurally improper. The Final DIP Order is final and can only be modified through a timely appeal or a motion to reconsider. The Committee in fact did appeal the Final DIP Order. *See* Notice of Appeal and Statement of Election, *In re Verity Health System of California, Inc., et al.*; 2:18-cv-10675-RGK [Dkt No. 1]. In its Notice of Appeal, the Committee sought to overturn Paragraphs 2(d), 2(h), 5(d), 5(f), 19 and 28(e) of the Final DIP Order. The Committee chose not to appeal Paragraph 5(e). If the language "mistakenly suggested that Defendant has a perfected security interest in all of the assets of all of the Debtors," the Committee could have raised this when it filed

its initial Notice of Appeal. As described in paragraph 28 hereof, the Committee's appeal has now been decided by the District Court, and the Committee has further appealed the District Court's decision to the Ninth Circuit Court of Appeals. The Committee cannot now seek to challenge or modify the provisions of the Final DIP Order through its Complaint.

Finally, to the extent that the Committee believed that there was an error in the Court's Final DIP Order, it was required to timely seek relief under Federal Rule of Civil Procedure 60(b)(1), incorporated under Federal Rule of Bankruptcy Procedure 9024, but the Committee did not do so.

**CONCLUSION**

For the foregoing reasons, the Notes Trustee respectfully requests that the Court grant its Motion to dismiss the Amended Complaint.

Dated: September 30, 2019

**MCDERMOTT WILL & EMERY LLP**

By: /s/ *Jason D. Strabo*
Jason D. Strabo

**MASLON LLP**

By: /s/ *Clark T. Whitmore*
Clark T. Whitmore

*Attorneys for U.S. Bank National Association, not individually but as Notes Trustee*

DM_US 163078832-1.083507.0011

# PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this adversary proceeding. My business address is: McDermott Will & Emery LLP, 2049 Century Park East, Suite 3200, Los Angeles, CA 90067-3206.

A true and correct copy of the foregoing document, entitled NOTES TRUSTEE'S MOTION TO DISMISS AMENDED COMPLAINT, MEMORANDUM IN SUPPORT THEREOF, will be served or was served (a) on the judge in chambers in the form and manner required by LBR 5005-2(d); and (b) in the manner stated below:

**1**. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**: Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On September 30, 2019, I checked the CM/ECF docket for this bankruptcy case and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

Mark Shinderman, Robert J. Liubicic, Alexandra Achamallah, James Cornell Behrens, Thomas E. Jeffry Jr., and Robert M. Hirsh on behalf of the Official Committee of Unsecured Creditors of Verity Health System of California, Inc., et al.
mshinderman@milbank.com, rliubicics@milbank.com, aachamallah@milbank.com, jbehrens@milbank.com, thomas.jeffry@arentfox.com, robert.hirsch@arentfox.com

Samuel R. Maizel, Tania M. Moyron and Nicholas A. Koffroth on behalf of Debtors Verity Health System of California, Inc., et al.
samuel.maizel@dentons.com, tania.moyron@dentons.com, nick.koffroth@dentons.com

United States Trustee (LA) ustpregion16.la.ecf@usdoj.gov

☐ Service information continued on attached page

**2. SERVED BY UNITED STATES MAIL**:
On _____, 2019, I served the following persons and/or entities at the last known addresses in this bankruptcy case by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

☐ Service information continued on attached page

**3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL** (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on September 30, 2019, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

**Via Personal Delivery:**
Honorable Ernest Robles
United States Bankruptcy Court for the Central District of California
Roybal Federal Building
255 E. Temple Street, Suite 1560
Los Angeles, CA 90012

☐ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

| September 30, 2019 | Jason D. Strabo | */s/ Jason D. Strabo* |
|---|---|---|
| *Date* | *Printed Name* | *Signature* |

Jason D. Strabo (SBN 246426)
McDermott Will & Emery LLP
2049 Century Park East, Suite 3200
Los Angeles, CA 90067-3206
Telephone: 310.788.4125
Facsimile: 310.277.4730
Email: jstrabo@mwe.com

Nathan F. Coco (admitted pro hac vice)
Megan Preusker (admitted pro hac vice)
McDermott Will & Emery LLP
444 West Lake Street, Suite 4000
Chicago, IL 60606-0029
Telephone: 312.372.2000
Facsimile: 312.984.7700
Email: ncoco@mwe.com
mpreusker@mwe.com

Clark T. Whitmore (admitted pro hac vice)
Jason M. Reed (admitted pro hac vice)
Maslon LLP
90 S. 7th Street, Suite 3300
Minneapolis, MN 55402
Telephone: 612.672.8200
Facsimile: 612.642.8301
Email: clark.whitmore@maslon.com
jason.reed@maslon.com

*Attorneys for U.S. Bank National Association, not individually but as Notes Trustee*

**UNITED STATES BANKRUPTCY COURT**
**CENTRAL DISTRICT OF CALIFORNIA**
**LOS ANGELES DIVISION**

| | |
|---|---|
| In re:<br><br>VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*,<br><br>Debtors. | Lead Case No. 2:18-bk-20151-ER<br><br>Chapter 11<br><br>Adv. Proc. No. 2:19-ap-01165-ER |
| OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*,<br><br>Plaintiff,<br><br>v.<br><br>U.S. BANK NATIONAL ASSOCIATION, as Trustee,<br><br>Defendant. | **REPLY IN SUPPORT OF MOTION OF U.S. BANK NATIONAL ASSOCIATION, AS NOTES TRUSTEE, TO DISMISS AMENDED COMPLAINT**<br><br>Date: November 21, 2019<br>Time: 10:00 am<br>Judge: Hon. Ernest M. Robles<br>Place: U.S. Bankruptcy Court<br>Courtroom 1568<br>Edward R. Roybal Federal Building<br>255 East Temple Street<br>Los Angeles, CA 90012 |

**TABLE OF CONTENTS**

# TABLE OF AUTHORITIES

## I. INTRODUCTION

The Notes Trustee,[1] in its Motion to Dismiss, has moved to dismiss each of the four Counts set forth in the Committee's Amended Complaint on the grounds that, *inter alia*, (1) they have been waived and/or are time barred (Counts I, II, III & IV), (2) the Committee lacks standing to raise Challenges regarding post-petition assets because that goes beyond the scope of prepetition lien challenges identified in section 5(e) of the Final DIP Order (Counts I, III & IV) , (3) there is no justiciable controversy (Count II), (4) they fail to meet minimum pleading requirements, particularly the Committee's conclusory categorical assertion there were no "identifiable cash proceeds" in the Hospital Debtors' Deposit Accounts (Count II), and (5) the Committee's request for a conditional determination that the Notes Trustee is undersecured runs afoul the Court's uncontroverted finding that the Prepetition Secured Creditors were oversecured as of the Petition Date with an equity cushion of between $150 and $200 million (Count IV). *See* Tentative Ruling, p. 8.

In its Opposition, the Committee asserts that all of its new lien challenge theories and claims are "appropriate and timely" because its Original Complaint employed the term "including." *See* Opposition, p. 6. The Committee posits that the use of the word "including" in the Original Complaint somehow overrides the effect of the Challenge Deadline Deadlines in December 2018 and June 2019 under the Final DIP Order and entitles Committee to assert countless new additional lien Challenges to the Notes Trustee's Prepetition Liens long after the Challenge Deadline has lapsed, even though the new lien challenge theories and claims were not referenced or preserved under the Challenge Stipulations entered into by the Committee and Notes Trustee.

Similarly, the Committee asserts that the Court's uncontroverted factual findings in the Tentative Ruling regarding the value of the Debtors' assets and the oversecured nature of the Prepetition Secured Creditors' claims may now be challenged and circumscribed in this adversary proceeding because the Court's findings were "subject to" the Committee's ever-evolving lien challenge rights under Section 5(e). In other words, according to the Committee, the Final DIP Order is not really a *final* order at all, because its terms and the Court's factual findings with respect

[1] Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to them in the Motion to Dismiss, the Final DIP Order and the Supplemental Cash Collateral Order, as applicable.

thereto are all subject to re-litigation by the Committee on the eve of Plan conformation. However, the Final DIP Order, itself, states it is binding and enforceable, and that its findings are immediately effective and enforceable. *See* Final DIP Order, ¶¶ 28(b) & 29(b).

The Committee's ever-evolving lien challenges in this adversary proceeding cannot be divorced from the larger context of the Debtors' chapter 11 cases. As both the Court and the Committee have observed, the Debtors are suffering operating losses of approximately $450,000 per day.[2] Keeping the Hospitals operational during these chapter 11 cases, in the face of the staggering financial losses, has only been made possible because the Debtors' Prepetition Secured Creditors, including the Notes Trustee, (a) permitted their perfected prepetition liens to be primed by a $185 million DIP facility, and (b) consented to the use of hundreds of millions of dollars of their cash collateral throughout the course of the bankruptcy cases to fund operating losses, pay administrative expenses, and ultimately repay the DIP Loan itself. The Notes Trustee did so in direct reliance upon the finality of the Final DIP Order and the Court's predicate findings therein. *See* Final DIP Order, ¶ 28(a) (stating that "the Prepetition Secured Creditors … have acted in good faith in connection with … authorizing use of Cash Collateral and rely on this Final Order in good faith"). Now, at the final stages of these chapter 11 cases, the Committee is attempting to subvert the protections granted to the Notes Trustee in the Final DIP Order by raising new untimely lien challenges and collaterally attacking the Court's uncontroverted factual findings in connection therewith in an effort to forestall confirmation of the Debtors' proposed plan. The Committee's attempt to re-litigate the Final DIP Order and its factual underpinnings under the guise of a lien challenge, more than a year after the order was entered, must be rejected.

[2] *See Memorandum of Decision Granting Debtors' Emergency Motion To Enforce The Sale Order* (Docket No. 3446) p. 3; *Official Committee of Unsecured Creditors' Response in Support of Debtors' Emergency Motion for the Entry of an Order: (I) Enforcing the Order Authorizing the Sale to Strategic Global Management, Inc.; (II) Finding That the Sale is Free and Clear of Conditions Materially Different Than Those Approved by the Court; and Other Relief* (Docket No. 3320), p. 3.

## II. ARGUMENT

### A. The Committee's New Lien Challenges Under the Amended Complaint Have Been Expressly Waived by the Committee and/or are Otherwise Time Barred

As detailed in the Notes Trustee's Motion to Dismiss, the new lien challenge claims and theories, raised for the first time in the Committee's Amended Complaint filed after the Challenge Deadline, were waived by the Committee and should be dismissed. The Final DIP Order granted the Committee limited standing to initiate a "Challenge" with respect to "the validity, enforceability and amount of the Prepetition Secured Obligation and the Prepetition Liens" on or before the "Challenge Deadline." Final DIP Order, ¶ 5(e). The initial Challenge Deadline of December 13, 2018 was subsequently extended to June 13, 2019 through a series of stipulations entered into by the Committee and Notes Trustee. As consideration for the extension of the Challenge Deadline, the Committee stipulated and agreed that the original Challenge Deadline would *not* be extended with respect to "Acknowledged Collateral," a defined term in the Challenge Stipulation that includes, *inter alia*:

- "perfected deed of trust liens and security interests in the real property";
- "perfected deed of trust liens and security interests in the *Facilities*, Appurtenances, Equipment, Leases, Rents, *Proceeds* and Inventory of St. Francis Medical Center, Saint Louise Regional Hospital and Verity Holdings LLC";
- "Accounts (as defined in the Security Agreements referred to in the Loan Agreements)";
- "All *products*, *replacements* and *Proceeds*" of the foregoing; and
- "a perfected security interest in the deposit accounts set forth on Exhibit B" thereto.

Challenge Stipulation, p. 2 (emphasis added).

The Term "Accounts" – with respect to which the Committee's lien challenge rights were expressly waived – was defined to include, *inter alia*,

- "any right to payment of a monetary obligation whether or not earned by performance, that relates to or arises out of any services provided or goods rendered by an Obligated Group Member";
- "any 'account' (as defined in the UCC), any accounts receivable, whether in the form of payments for services rendered or goods sold, rents, license fees or otherwise, any Health-Care-Insurance Receivables (as defined in the UCC)";

- "Payment Intangibles (as defined in the UCC)";
- "General Intangibles"; and
- "all *proceeds* of any of the foregoing"

Security Agreement, Schedule V.

Notwithstanding the stipulated waiver of these broad categories of liens and security interests – constituting virtually the entire lien position of the Notes Trustee, including the proceeds, products and replacements thereof – the Committee subsequently filed its Original Complaint in June of 2019 purporting to challenge the validity of Notes Trustee's liens upon and security interests in the *proceeds* of the Debtors' Accounts (which were held in the Debtors' Deposit Accounts). *See* Original Complaint, ¶ 33 (asserting that funds in certain Deposit Accounts "do not constitute identifiable cash *proceeds* of an otherwise perfected, unavoidable lien in other collateral of the Defendant") (emphasis added). As detailed in the Motion to Dismiss, any challenge to the validity of the Notes Trustee's security interest in the proceeds and products of the Accounts and other Acknowledged Collateral was expressly waived by the Committee under the Challenge Stipulation and is time barred under the Final DIP Order.

Then, nearly three months *after* the expiration of the June 13, 2019 Challenge Deadline, the Committee compounded its waiver problem by amending its Original Complaint to raise several wholly new lien challenge theories and claims for the first time, in violation of the Challenge Stipulation. These include (1) a new request in Count I for a declaration that the Notes Trustee does not have a perfected security interest in "any going concern premium that has been or will be generated" from the sale of encumbered assets (including Acknowledged Collateral), (2) a new request in Count I for a declaration that the Notes Trustee does not have a perfected security interest in MOB Assets (which is facially incorrect as to the Moss Blvd. Deed of Trust), (3) a new fraudulent conveyance claim in Count III conditionally seeking to avoid any loan agreement amendments that may have captured a valid lien on Future QAF Disbursements and; and (4) a new Count IV seeking a

declaration that the Notes Trustee would be undersecured if the Court were to agree with the Committee's positions. None of these new lien challenge theories and claims survived the Challenge Stipulation. Nor were they included in the Original Complaint (*i.e.*, filed before the lapse of the Challenge Deadline).

As indicated in the Motion to Dismiss, the Committee's new theories and claims are not proper lien Challenges for which the Committee has standing, they have not been properly pled and they have procedural defects. But, even if they were not otherwise subject to dismissal, these new lien challenge claims have been raised too late, the Challenge Deadline having expired, and are therefore waived and time barred. In fact, the new cause of action inserted as Count IV in the Amended Complaint (*i.e.*, the requested declaration that the Notes Trustee is undersecured) falls squarely within the original time limitation provision set forth in section 5(e) of the Final DIP Order:

> the "Challenge Deadline" for matters solely relating to the *value* of the Prepetition Collateral may be further extended to such time as may be agreed by stipulation among the Debtors, the Committee and the Prepetition Secured Creditors or as further ordered by the Court.

Final DIP Order, ¶ 5(e) (emphasis added).

The Challenge Stipulation plainly states that, "[i]n consideration of the extension of the Challenge Deadline for certain assets of the Debtors as provided hereinbelow, the Committee Acknowledges that the Challenge Deadline shall not be extended for the Acknowledged Collateral." Challenge Stipulation, ¶ A. In its Opposition, the Committee acknowledges that it "was obligated to pursue an action or be forever barred from doing so." Opposition, p. 12. This is precisely what happened. The Committee's intention to allow the Challenge Period to expire for Acknowledged Collateral is manifest in the Challenge Stipulation.

In its Opposition, the Committee argues that the new lien challenge claims added to its Complaint after the expiration of the June 13, 2019 Challenge Deadline are not time barred because they "relate back" to the claims delineated in the Original Complaint. This is not even responsive to

the lien challenge claims which expired in December 2018 by reason of the Court-approved Challenge Stipulation. Moreover, the Original Complaint never mentioned, let alone addressed, (1) the "MOB Assets," (2) any so-called "going concern premium," (3) fraudulent conveyance claims related to Future QAF Disbursements, or (4) the value or oversecured nature of the Notes Trustee's Prepetition Liens on Prepetition Collateral, nor were any of these new lien challenge claims referenced or preserved in the Challenge Stipulation entered into by the Committee and Notes Trustee and approved by the Court. These new claims were raised for the first time in the Committee's Amended Complaint. Under FRCP 15(c), a new claim added to a complaint "relates back" to the original claim only to the extent that "the new claim relies on the same facts and does not seek to insert new facts." *In re Magno*, 216 B.R. 34, 41 (B.A.P. 9th Cir. 1997). *See also Echlin v. PeaceHealth*, 887 F.3d 967, 978 (9th Cir. 2018) ("claims must share a common core of operative facts such that the plaintiff will rely on the same evidence to prove each claim. Thus, an amendment will not relate back when the amended complaint had to include additional facts to support the new claim"). None of the Committee's newly added lien challenge claims "relate back" to the Original Complaint because each necessarily involves new factual predicates and allegations, new legal theories, and additional forms of relief:

- The Committee's new legal claim with respect to the so-called "going concern premium" requires adjudication of a multitude of new factual matters which were not alleged in the Original Complaint, including testimonial and documentary evidence regarding (i) the existence and quantification of any such "going concern premium," (ii) the allocation of any such "going concern premium" as between or among the various Hospital Debtors, (iii) the allocation of any such "going concern premium" to the various asset classes and collateral categories identified in the Notes Trustee's Security Agreements, (iv) the quantification and attribution of the alleged "going concern premium," if any, to the Debtor's labor force, *etc.*

- The Committee's new legal claim with respect to the MOB Assets requires adjudication of new factual matters regarding, *inter alia*, (i) the valuation of the MOB Assets, (ii) the existence of any other liens or security interests on such assets, (iii) the quantification of any Diminution in Value and associated Replacement Lien held by the Notes Trustee on such assets, *etc.*

- The Committee's new fraudulent conveyance claim with respect to Future QAF Disbursements requires adjudication of new factual matters regarding, *inter alia*, (i) the solvency and capitalization of the Debtors at the time the loan and security documents were allegedly modified, (ii) whether such modifications constituted a "transfer" under the governing statutory provisions, (iii) the existence and quantification of any reasonably equivalent value associated with any such transfer, (iv) whether any such transfer is subject to a good faith or other legal or equitable defense under the governing statutes, *etc.*

- The Committee's new legal claim with respect to the supposed undersecured nature of the Notes Trustee's claims requires adjudication of new factual matters, including testimonial and documentary evidence regarding, *inter alia*, (i) the valuation of all real and personal property collateral pledged to the Notes Trustee, (ii) the existence and quantification of any alleged "going concern premium," (iii) the quantification of any Diminution in Value and associated Replacement Lien held by the Notes Trustee on any unencumbered or junior pre-petition or post-petition assets of the Debtors, (iv) the quantitative difference between the going concern value of the Debtor' assets and the hypothetical liquidation value, *etc*.

According to the Committee, the Challenge Deadline and other related limitations set forth in Section 5(e) of the Final DIP Order are rendered moot or meaningless by virtue of the fact that the Original Complaint employed the term "including." Through its use of the term "including," the Committee posits that it is entitled to assert countless new additional lien Challenges to the Notes Trustee's Prepetition Liens long after the Challenge Deadline has lapsed. This line of argument is specious; the Committee's use of the word "including" did not toll the Challenge Deadline under the Court's Final DIP Order. To argue otherwise would suggest that the Challenge Stipulation, itself, was somehow superfluous.

The Committee also asserts in its Opposition that the waiver issue is not appropriate for adjudication in connection with a motion to dismiss. *See* Opposition, pp. 14-15. The cases cited by the Committee are inapposite because the waiver issue here does not invite or require extraneous evidence; it merely requires the interpretation and application of the Final DIP Order, the Challenge Stipulation, and the Amended Complaint. Each of these documents is clear and unambiguous with respect to the applicable Challenge Deadline. Accordingly, the waiver / timeliness issue can and should be decided upon the basis of the Motion to Dismiss. A Rule 12(b)(6) motion to dismiss based upon the untimeliness of a claim may be granted when it is clear from the pleadings that the

claims being brought are untimely. *See Seven Arts Filmed Entertainment Ltd. v. Content Media Corp. PLC*, 733 F.3d 1251 (9th Cir. 2013). No further factual development is needed here.

In short, the new lien challenge theories and claims asserted by the Committee in the Amended Complaint, brought after the Challenge Deadline expired, are waived, time barred and should be dismissed.

**B. The Committee's Untimely Challenge to the Value of the Notes Trustee's Collateral Constitutes an Improper Collateral Attack on this Court's Findings in the Tentative Ruling**

As detailed in the Notes Trustee's Motion to Dismiss, the Committee's new Count IV is not only untimely as a Challenge, it constitutes an improper collateral attack on the Court's prior finding that the Notes Trustee and the other Prepetition Secured Creditors are oversecured.

On October 3, 2018, this Court issued its Tentative Ruling on the Debtors' DIP Motion (Docket. No. 392). In the Tentative Ruling, the Court expressly found, as an uncontroverted factual and evidentiary matter, that the Notes Trustee and the other Prepetition Secured Creditors were oversecured with an equity cushion of between $150 and $200 million:

> Based upon its review of the declarations of James Moloney and Anita Chou, the Court finds that the Debtor has submitted competent evidence establishing the need for the proposed financing from the DIP Lender. Specifically, as of the Petition Date, the book value of the Debtors' assets was approximately $857 million. Moloney Decl. [Doc. No. 309] at ¶8. After proper marketing, the aggregate realizable value of those same assets is in the range of $725 million to $800 million. Id. As of the Petition Date, aggregate secured claims against the Debtors totaled approximately $565 million. Id. at ¶9. The realizable value of the Debtors' assets, in excess of prepetition secured liabilities, is between $150–$225 million. Id. During the first thirteen weeks of the case, the Debtors are projected to collect approximately $239 million in patient revenue, but spend approximately $405 million to maintain operations. Chou Decl. [Doc. No. 309], Ex. 1. The total cash shortfall during the first thirteen weeks is approximately $109 million. *Id*. These figures establish that the Debtors are in dire need of post-petition financing. If the Debtors continue operations, they have a realistic opportunity to sell their assets for a price that will yield between $150–$225 million in excess of existing secured debt. A sale at that price would result in a meaningful recovery for unsecured creditors. However, simply to maintain operations over the first thirteen weeks of the case, the Debtors must plug a funding shortfall in excess of $100 million. Against this backdrop, the Court finds it appropriate to approve the financing package that the Debtors have negotiated with the DIP Lender. In this respect, the Court notes that secured creditors holding a significant portion of the outstanding secured indebtedness also support the proposed financing.

Tentative Ruling, p. 8. In short, the Court made adjudicated factual findings that the going concern value of the Debtors' assets subject to the Prepetition Secured Creditor's liens in this case was $725 to $800 million, and that the total secured debt was $565 million, thereby resulting in an equity cushion of $150 to $225 million. *Id.*

Notably, the Committee actively participated in the Final Hearing on the DIP Motion, and even prosecuted a number of objections to the entry of the Final DIP Order, which objections were overruled by the Court. But the Committee never contested the Court's factual and evidentiary findings that the Notes Trustee was oversecured and, likewise, never contested that the Notes Trustee was entitled to a Prepetition Replacement Lien on all of the Debtors' assets as protection against a Diminution in Value of its equity cushion. At the final hearing, the Court considered evidence submitted by the Debtors in the form of evidentiary declarations from a number of management level individuals employed by the Debtors and their professionals. No party, including the Committee, objected to the evidence presented in support of the DIP Motion. No party, including the Committee, introduced evidence that contradicted or rebutted any of the evidence or facts presented in connection with the DIP Motion. No party, including the Committee, objected to or challenged the Court's use of going concern value (as opposed to foreclosure value or some other metric) with respect to the Prepetition Collateral and the Prepetition Secured Creditors equity cushion therein.

Following the entry of the Final DIP Order, the Committee did not appeal the Court's findings regarding the valuation of the Prepetition Secured Creditors' claims and equity cushion, nor the Court's conclusion that the Prepetition Secured Creditors were oversecured. The Committee filed an appeal solely with respect to the waivers of the "equities of the case" exception to Section 552(b) and the trustee surcharge rights under Section 506(c) of the Bankruptcy Code, but not with respect to valuation.

In its Opposition, the Committee asserts that the Court's uncontroverted factual findings in the Tentative Ruling regarding the value of the Debtors' assets and the oversecured nature of the Prepetition Secured Creditors' claims may now be challenged and circumscribed in this adversary proceeding because the Court's findings were "subject to" the Committee's ever-evolving lien

challenge rights under Section 5(e). In other words, according to the Committee, the Final DIP Order is not really a *final* order at all, because its terms and the Court's factual findings with respect thereto are all subject to re-litigation by the Committee on the eve of Plan conformation. However, the Final DIP Order, itself, states that it is binding and enforceable, and that its findings are immediately effective and enforceable. *See* Final DIP Order, ¶¶ 28(b) ("The provisions of this Final Order shall be binding upon and inure to the benefit of the DIP Agent, DIP Lender, the Debtors, the Prepetition Secured Creditors, McKesson, the Committee, all other Parties in Interest, and all creditors, and each of their respective successors and assigns") & 29(b) ("This Final Order shall constitute findings of fact and conclusions of law pursuant to the Bankruptcy Rule 7052 and shall take effect and be fully enforceable *nunc pro tunc* to the Petition Date immediately upon entry of this Final Order").

The Committee's argument that the Court's findings in the Tentative Ruling are not true factual findings but, instead, mere provisional suggestions "subject to" later challenge and re-litigation by the Committee is further belied by the fact that those findings formed the basis for the Court's decision therein to *overrule* the Committee's various objections to the Final DIP Order itself.! *See* Tentative Ruling, pp. 10-12 ("The Objections Asserted by the Committee are Overruled"). Obviously, the lien challenge rights set forth in section 5(e) of the Final DIP Order relate to the specific factual stipulations made by the Debtors in that provision, and cannot be reasonably construed to override the Court's own separate and independently-derived factual findings in the Tentative Ruling, including the Court's findings resulting in the overrule the Committee's objections to the Final DIP Order. Were it otherwise, the Committee arguably would not have even needed to appeal the Final DIP Order at all, but merely repackage its failed objections to the Court's prior findings as a lien challenge.

In its Opposition, the Committee improperly conflates its right to challenge the Debtors' stipulations in section 5(e) of the Final DIP Order regarding the validity, enforceability and amount of the Prepetition Obligations and Prepetition Liens with the Court's adjudicated findings in the Tentative Ruling. The Court's asset valuation findings proceed from the Court's independent assessment of evidence at a contested hearing, not its incorporation of the Debtors' deal into findings

that can be challenged by creditors (including the Committee) who were not included in the deal. The Prepetition Secured Creditors have relied upon the Court's evidentiary findings as the adjudicated basis for the value of the Debtors' assets as of the Petition Date and the adequacy of the Replacement Liens included as adequate protection in the Final DIP Order. Read in context, section 5(e) did not grant to the Committee the right to ignore the Court's evidentiary findings (to which it did not bother to rebut at the Final Hearing) of the Court incorporated from the Tentative Ruling. Importantly, section 28(a) of the Final DIP Order states that:

> The Debtors, the DIP Agent, the DIP Lender, the Prepetition Secured Creditors and McKesson have acted in good faith in connection with negotiating the DIP Financing Agreements, extending credit under the DIP Facility, and authorizing use of Cash Collateral and rely on this Final Order in good faith. Based on the findings set forth in this Final Order and the record made during the Interim Hearing and the Final Hearing, and in accordance with section 364(e) of the Bankruptcy Code, *in the event any or all of the provisions of this Final Order are hereafter reversed, modified amended or vacated by a subsequent order of this or any other Court*, *the* DIP Agent, DIP Lender, *Prepetition Secured Creditors* and McKesson *are entitled to the protections provided in section 364(e) of the Bankruptcy Code. Any such reversal, modification, amendment or vacatur shall not* affect the validity and enforceability of any advances made pursuant to this Final Order or the DIP Financing Agreements, nor shall it *affect the validity, priority, enforceability, or perfection* of the DIP Liens, *the Prepetition Replacement Liens* or the VMF Replacement Lien. *Any* claims or DIP Protections granted to the DIP Agent and the DIP Lender hereunder, or *adequate protection granted to the Prepetition Secured Creditors* and McKesson hereunder, *arising prior to the effective date of such reversal, modification, amendment or vacatur, shall be governed in all respects by the original provisions of this Final Order, and the* DIP Agent, the DIP Lender, *Prepetition Secured Creditors* and McKesson *shall be entitled to all of the rights, remedies, privileges and benefits, including the* DIP Protections and *adequate protection granted herein, with respect to any such claims.* Since the loans made pursuant to the DIP Credit Agreement are made in reliance on this Final Order, the obligations owed to the DIP Agent, the DIP Lender, the Prepetition Secured Creditors or McKesson prior to the effective date of any reversal or modification of this Final Order cannot, as a result of any subsequent order in the Chapter 11 Cases or in any Successor Cases, be subordinated, lose their lien priority or superpriority administrative expense claim status, or be deprived of the benefit of the status of the liens and claims granted to the DIP Agent, the DIP Lender, the Prepetition Secured Creditors or McKesson under this Final Order and/or the DIP Financing Agreements.

Final DIP Order, ¶ 28(a) (emphasis added). Accordingly, if the Court permits the Committee to attack the Final DIP Order's adjudicated value findings at this stage (and it should not), the existing form of the Final DIP Order, including all such findings, should be applicable under Section 28 to any Diminution in Value that has occurred to that date.

Finally, the Committee asserts that, if it is not permitted to now challenge the Court's prior finding in the Tentative Ruling that the Notes Trustee is oversecured, "the Challenge Right would be meaningless" and so "why have a Challenge Right at all?" Opposition, p. 2. The Committee's rhetorical question misses the point: It had the opportunity to challenge the valuation evidence presented at the Final Hearing on the DIP Motion but it chose not to do so. It had the opportunity to introduce evidence or facts at the Final Hearing that contradicted or rebutted the valuation evidence presented by the Debtors but it chose not to do so. It had the opportunity at the Final Hearing to object to or challenge the Court's use of going concern value (as opposed to foreclosure value or some other metric) with respect to the Prepetition Collateral and the Prepetition Secured Creditors' equity cushion therein but it chose not to do so. It had the opportunity to appeal the Court's findings in the Tentative Ruling that the Prepetition Creditors were oversecured but did not do so. The Committee had the opportunity to otherwise raise certain of its other new lien challenge theories and claims *before* the expiration of Challenge Deadline but it chose not to do so. Instead, it waited until the end of the chapter 11 cases to raise these issues for the first time, notwithstanding the fact that the very purpose of the lien challenge provision in section 5(e) of the Final DIP Order was to timely flesh-out and adjudicate any such issues early on in the case.

### C. The Court Should Dismiss Count II of the Amended Complaint as Failing to Present Justiciable Issues

As detailed in the Notes Trustee's Motion to Dismiss, Count II of the Amended Complaint fails to present a real case or controversy because the Committee fails to allege that any real money is at stake. The Court found in the Final DIP Order that the Notes Trustee and other Prepetition Secured Creditors are entitled to a Prepetition Replacement Lien in all DIP Collateral to the extent of any Diminution in Value, including any otherwise unencumbered Deposit Accounts. Moreover, the funds in the subject Deposit Accounts have already been spent by the Debtors along with hundreds of millions of dollars of the Notes Trustee's other cash collateral.

The Committee defends the need for litigation on Count II even though there are no funds to fight over on the grounds that the outcome could be helpful in fixing the amount of the Notes Trustee's prepetition claim for purposes of later Diminution in Value litigation. A fight involving

experts and tracing is not justified by this end, and this issue could be litigated more efficiently in connection with confirmation if relevant to the fully secured status of the Notes Trustee. Again, this dispute is unripe as it really relates to the Diminution in Value issues not presented in the adversary proceeding.

**D. The Committee's Arguments Regarding the Merits of its so-called "Going Concern Premium" Theory are Premature and Should be Disregarded**

The Notes Trustee, in its Motion to Dismiss, argued that the Committee's new claim regarding the so-called "going concern premium" should be dismissed because, *inter alia*, it goes beyond the scope of the enumerated challenges identified in section 5(e) of the Final DIP Order, and section 5(e) does not contemplate lien challenge claims or causes of action related to postpetition matters. The Notes Trustee has not sought dismissal of the Committee's "going concern premium" theory based on the legal or factual merits thereof, but rather with respect to standing and waiver. However, in order to avoid any misapprehensions about the Notes Trustee's position with respect to the Committee's "going concern premium" argument, the Notes Trustee stated in a footnote to its Motion to Dismiss that the argument is contrary to both the Final DIP Order and binding precedent in the Ninth Circuit on the proper valuation of collateral sold as part of a going concern, citing *In re Sunnyslope Housing L.P.*, 859 F.3d 637 (9th Cir. 2017). *See* Motion to Dismiss, n. 9. In its Opposition, the Committee responds the footnote with a five page exposition of its legal theory. *See* Opposition, pp. 15-20.

The Committee's arguments in favor of the "going concern premium" theory are, for purposes of this adversary proceeding, premature, irrelevant to the Motion to Dismiss, and are perhaps more appropriately addressed in the context of the confirmation of the Debtors' Plan. Nonetheless, just so the record is clear, the Notes Trustee believes that the Committee's "going concern premium" theory lacks substantive merit and reserves its right to brief and adjudicate that issue at the appropriate time. Suffice it to say that there is no "going concern premium" as a separate, distinct, and unencumbered asset class that inures solely to the benefit of unsecured creditors, and the cases cited by the Committee do not stand for that proposition. As one court in this Circuit has observed, "[t]here is no precedent that supports the conclusion that a secured creditor

with a lien on a debtor's primary assets is not entitled to the debtor's enterprise value when the debtor proposed to use that collateral in its business under a plan of reorganization." *In re Hawaiian Telcom Commc'ns, Inc.*, 430 B.R. 564, 604 (Bankr. D. Haw. 2009).

## III. CONCLUSION

For the foregoing reasons, the Notes Trustee respectfully reiterates its request that the Court grant its Motion to Dismiss the Amended Complaint.

Dated: October 24, 2019

**MCDERMOTT WILL & EMERY LLP**

By: /s/ *Jason D. Strabo*
Jason D. Strabo

**MASLON LLP**

By: /s/ *Clark T. Whitmore*
Clark T. Whitmore

*Attorneys for U.S. Bank National Association, not individually but as Notes Trustee*