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Attorneys for Retirement Plan for Hospital Employees

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 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 Robles

**OBJECTION OF RETIREMENT PLAN
FOR HOSPITAL EMPLOYEES TO
MOTION OF DEBTORS FOR FINAL ORDERS
(A) AUTHORIZING THE DEBTORS TO
OBTAIN POST PETITION FINANCING ETC.,**

Final Hearing:

Date: October 3, 2018

Time: 10:00 a.m. (PST)

Place: United States Bankruptcy Court
255 East Temple Street
Suite 90012
Los Angeles, California 90012

TrodeLLa & Lapping LLP
540 Pacific Avenue
San Francisco, CA 94133

TO THE COURT AND ALL PARTIES AND THEIR ATTORNEYS OF RECORD:

Retirement Plan for Hospital Employees (“RPHE”) hereby files this objection to 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 110* [Docket No. 31] (the “Financing Motion”) filed by Verity Health System Of California, Inc. (“VHS”) and the above-referenced affiliated debtors, the debtors and debtors in possession in the above-captioned chapter 11 bankruptcy cases (collectively, the “Debtors”), as follows:

BACKGROUND

RPHE is a multiemployer qualified defined benefit retirement plan under Section 401(a) of the Internal Revenue Code. VHS and certain of its affiliates, O'Connor Hospital, Saint Louise Regional Hospital, and Seton Medical Center, including Seton Medical Center Coastsides, are participants in RPHE and pursuant to collective bargaining agreements (“CBAs”) with the California Nurses Association (“CNA”), are obligated to make contributions to RPHE on behalf of members of CNA currently working at the above facilities. (Declaration of Michael Holdsworth, para. 2.)

Under the terms of the RPHE Trust Agreement and the Plan Document and Summary Plan Description applicable to VHS and its affiliates, IRS rules, and actuarial determinations, RPHE issues an annual Invoice to VHS requiring payment of the previous year’s accrued contributions in three installments, due on February 15, May 15 and August 15 of the following calendar year. Thus, for 2017 contributions, RPHE issued Invoices to VHS for February 15, 2018 in the amount of \$4,791,218, for May 15, 2018 in the amount of \$4,791,218, and for August 15, 2018 in the amount of \$4,791,217. VHS paid the February 15 and May 15 Invoices, but did not pay the Invoice for August 15. (Declaration of Michael Holdsworth, para. 3.)

Although RPHE has not issued VHS any Invoices for 2018, the contribution obligations continue to accrue, and have accrued for 8 months through August 31, 2018, the petition date. Thus, RPHE will have an unsecured prepetition claim for the August 15, 2018 Invoice (related to

2017 accruals) plus the accrued contributions for January through August, 2018. From and after September 1, 2018, VHS's contribution obligations will accrue continuously post-petition as part of the benefits earned by CNA members who staff the VHS facilities, even though in the ordinary course RPHE would not bill for any 2018 accrued contributions until the three scheduled dates in 2019. These contribution obligations are administrative expenses under 11 U.S.C. sections 503(b) and 507(a)(2). *See In re Pacific Far East Line, Inc.*, 713 F.2d 476 (9th Cir. 1983) (construing predecessor provision under the Bankruptcy Act). As such, these necessary expenses should be included in the DIP Budget described and attached to the Financing Motion. But they are not, as Debtors' counsel has informed counsel for RPHE.

OBJECTION

As RPHE understands the Debtors' position, the Financing Motion and the DIP Budget on which it is based, are objectionable for two reasons. First, although Debtors recognize that some portion of the annual Invoice to be issued in 2019 (for 2018) will be administrative expenses, they choose not to reserve for them in the budget until the 13-week rolling budget arrives at February 15, 2019, when the first Invoice for 2018 contributions will be issued—the timing problem. Second, the Debtors are not recognizing their obligations to contribute for Unfunded Actuarial Liability required under ERISA—the amount problem. Each will be addressed in turn.

A. Timing.

In the circumstances of these cases, all parties, including the secured creditors, recognize that without continued operations, the value of the estate plummets. Operations require employees, including CNA members, and the administrative expenses for operations must be accommodated in the financing structure. Here, if budgeted, they are accorded true priority, ahead of the DIP financing, which primes all others. But the DIP financing requires motions for sales of major assets and presumably repayment of the DIP financing, to commence within 60 days of the Petition Date, i.e., by October 31, 2018. (Condition (d), Financing Motion, Docket 31, p. 19.) If Debtors meet this schedule, or come close, then sales could close by year end and the DIP Budget become a thing of the past. Debtors will have received the benefit of the CNA members' work, but a major component of the expense will depend on the uncertain outcomes for unsecured

creditors in these cases. Moreover, including some benefits for some employees in the DIP Budget but not others, such as CNA members, is patently unfair and discriminatory as to CNA members.

RPHE objects to the approval of the Financing Motion unless it is contingent on adding accruals for the RPHE contributions in the DIP Budget.

B. Amount.

The contributions that Debtors are required to make to RPHE for any period fall into two categories. The first is based on the normal cost of benefits, the expected administrative expenses and a component of interest, all determined by IRS rules and actuarial determinations. The second category is Debtor's share of the Unfunded Actuarial Accrued Liability of the RPHE plan under ERISA, which is paid over a ten-year amortization. RPHE's actuarial estimate for these VHS contributions for Plan Year 2018 is attached as Exhibit A to the Declaration of Michael Holdsworth. As indicated on Exhibit A, the first category is \$1,756,757 for September 1 through December 31, 2018. Over 17 weeks for that period in the budget, this equals \$103,339 per week.

Based on discussions with Debtors' counsel, RPHE understands that Debtors will contend that only the first category will be recognized as an administrative expense. Thus, the second category, which is the Ten-year amortization of Unfunded Actuarial Accrued Liability of \$8,732,739, less the Withdrawn Employer Surplus Credit of \$1,101, 156, is \$7,631,583 for the entire year. Assuming straight line analysis, this equates to \$146,761 per week, or \$2,494,941 over the 17-week period to the end of 2018. These amounts are estimates subject to final calculation, although Debtor's actuaries appear to be extremely close on the numbers.

Unfunded Actuarial Accrued Liability is the result of the Actuarial Accrued Liability (for expected benefits owed to plan participants) exceeding the Actuarial Value of Assets in the plan, which can result from shortfalls in contributions or, more likely, fluctuations in the value of investments or legally required changes in actuarial assumptions (e.g., mortality). Although these amounts are measured by past, i.e., prepetition, events, they are nonetheless a current obligation under ERISA. *See Columbia Packing Co. v Pension Ben. Guaranty Corp.*, 81 B.R. 205, 18 CBC2d 1005 (D. Mass. 1988). In *Columbia*, the Pension Benefit Guaranty Corporation

1 (“PBGC”) sought administrative expense priority for “contributions which are sufficient to
2 eliminate any deficiencies in the account” of the applicable plan. The debtor urged that any part
3 of the current contribution obligation based on prepetition events should not have priority. As the
4 court put it, “[t]he principle [sic] issue, then, is whether the past service liability element of the
5 debtor's contribution should be given priority.” 81 B.R. at 207. The Court held that both
6 categories should be priority administrative expenses.

7 Here, as in *Pacific Far East* [713 F.2d 476 (9th Cir. 1983)], Columbia's
8 [the debtor's] obligation -- the past service liability cost -- was
9 calculated by reference to services performed before the priority period.
10 The obligation did not, however, accrue until after the priority period
11 began. More importantly, the contribution is owed to the pension fund
12 rather than the employees themselves. The past service liability cost is
13 more properly viewed as an actuarial unit of measure for determining
14 the employer's current periodic contribution than as compensation for
15 work performed before the inception of the plan.

16 81 B.R. at 208-09. In a footnote to the foregoing passage, the court observed:

17 Columbia argues that *Pacific Far East* is not relevant since, in this case,
18 the obligation arose at the inception of the plan year, before the priority
19 period. The Court disagrees. Under ERISA, the employer is required
20 to eliminate any accumulated funding deficiency by the end of the plan
21 year. 29 U.S.C. § 1082(a)(1). One could argue, then, that the
22 contribution is "due" on the last day of the plan year. A more realistic
23 view, under the circumstances, is to say that a pro rata portion of the
24 annual contribution accrues on a daily basis over the entire plan year.

25 81 B.R. at 209. This analysis underscore's RPHE's position that in chapter 11, the Debtor's
26 pension contributions must be deemed to accrue daily or weekly regardless of when they become
27 due outside of bankruptcy.

28 Thus, RPHE objects to the approval of the Financing Motion unless it is contingent on

1 adding accruals for the RPHE contributions in the DIP Budget in the amounts of \$103,339
2 (category 1) plus \$146,761 per week (category 2) or a total of \$250,100 per week to the end of
3 2018, with adjustments thereafter, subject to agreement to a final fine-tuning by the actuaries.

4 **CONCLUSION**

5 For the foregoing reasons, RPHE respectfully requests that the Court condition approval of
6 the Financing Motion on inclusion of a reserve fund for the RPHE plan contributions accruing in
7 2018 in the DIP Budget on a weekly basis in an amount to be determined by agreement or by
8 further proceedings if agreement cannot be reached.

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10 Dated: September 19, 2018

TRODELLA & LAPPING LLP

11
12 By: /s/ Richard A. Lapping
13 Richard A. Lapping
14 Attorneys for
15 Retirement Plan for Hospital Employees
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Trodella & Lapping LLP
540 Pacific Avenue
San Francisco, CA 94133

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:
540 Pacific Avenue, San Francisco, CA 94133

A true and correct copy of the foregoing document entitled (*specify*): OBJECTION OF RETIREMENT PLAN FOR HOSPITAL EMPLOYEES TO MOTION OF DEBTORS FOR FINAL ORDER (A) AUTHORIZING THE DEBTORS TO OBTAIN POST PETITION FINANCING ETC., and DECLARATION OF MICHAEL HOLDSWORTH IN SUPPORT OF OBJECTION, ETC.

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) 09/19/2018, 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

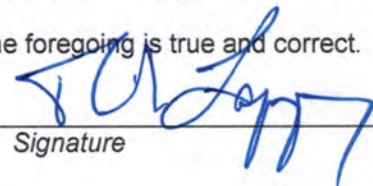
3. **SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL** (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on (date) 09/19/2018, I served the following persons and/or entities by personal delivery, overnight mail service, or (for 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.

☒ 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.

09/19/2018 Richard A. Lapping
Date Printed Name

Signature



Attachment to Proof of Service of Document

1. TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING(NEF)

Samuel R Maizel on behalf of Plaintiff Verity Health System of California, Inc.

samuel.maizel@dentons.com, alicia.aguilar@dentons.com;
docket.general.lit.LOS@dentons.com; tania.moyron@dentons.com;
kathryn.howard@dentons.com

Abigail V O'Brient on behalf of Creditor UMB Bank, N.A., as master indenture trustee and Wells Fargo Bank, National Association, as indenture trustee

avobrient@mintz.com, docketing@mintz.com; DEHashimoto@mintz.com; nleali@mintz.com

United States Trustee (LA)

ustpreion16.la.ecf@usdoj.gov

2. SERVED BY EMAIL

Counsel for the DIP Lender, Waller Lansden Dortch & Davis, LLP, 511 Union Street, Suite 2700, Nashville, TN 37219, Attn: David E. Lemke, Esq.

david.lemke@wallerlaw.com

Counsel to the Committee, Gregory A. Bray, Mark Shinderman, James C. Behrens, Milbank, Tweed, Hadley & McCloy LLP

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Counsel for U.S. Bank as 2015 Notes Trustee, McDermott, Will & Emory, 227 W. Monroe Street, Chicago, IL 60606-5096

Nathan F. Coco ncoco@mwe.com, Jason D. Strabo jstrabo@mwe.com,

Counsel for UMB Bank as successor Master Trustee, Mintz, Levin, Cohen, Ferris, Glovsky and Popeo PC, 1 Financial Center, Boston, MA 02111, Attn: Dan Bleck

DSBleck@mintz.com

United States Trustee (LA)

Jill.Sturdevant@usdoj.gov

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Attorneys for Retirement Plan for Hospital Employees

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 O'Connor Hospital
- ☐ Affects Saint Louise Regional Hospital
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- ☐ 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
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CASE NO.: 2:18-bk-20181-ER

Chapter 11 Cases

Hon. Judge Ernest Robles

**DECLARATION OF MICHAEL
HOLDSWORTH IN SUPPORT OF
OBJECTION OF RETIREMENT PLAN FOR
HOSPITAL EMPLOYEES TO MOTION OF
DEBTORS FOR FINAL ORDERS (A)
AUTHORIZING THE DEBTORS TO OBTAIN
POST PETITION FINANCING ETC.,**

Final Hearing:

Date: October 3, 2018

Time: 10:00 a.m. (PST)

Place: United States Bankruptcy Court

255 East Temple Street, Suite 90012
Los Angeles, California 90012

Trodella & Lapping LLP
540 Pacific Avenue
San Francisco, CA 94133

Trodella & Lapping LLP
540 Pacific Avenue
San Francisco, CA 94133

1
2 I, Michael Holdsworth, declare as follows:

3 1. I am the Chairman of the Board of Trustees of Retirement Plan for Hospital
4 Employees ("RPHE") and make this declaration in support of its objection to the Emergency
5 Motion Of Debtors *For Interim And Final Orders (A) Authorizing The Debtors To Obtain Post*
6 *Petition Financing (B) Authorizing The Debtors To Use Cash Collateral And (C) Granting*
7 *Adequate Protection To Prepetition Secured Creditors Pursuant To 11 U.S.C. §§ 105, 363, 364,*
8 *1107 And 110.* The matters stated herein are known to be to be true by personal knowledge and
9 observation, except where stated on information and belief, and as to those matters, I believe them
10 to be true. If called as a witness, I could and would testify competently to all matters set forth in
11 this declaration.

12 2. RPHE is a multiemployer qualified retirement plan under Section 401(a) of the
13 Internal Revenue Code. VHS and certain of its affiliates, O'Connor Hospital, Saint Louise
14 Regional Hospital, and Seton Medical Center, including Seton Medical Center Coastsides, are
15 participants in RPHE and pursuant to collective bargaining agreements ("CBAs") with the
16 California Nurses Association ("CNA"), are obligated to make contributions to RPHE on behalf
17 of members of CNA currently working at the above facilities.

18 3. Under the terms of the RPHE Trust Agreement and the Plan Document and
19 Summary Plan Description applicable to VHS and its affiliates, IRS rules, and actuarial
20 determinations, RPHE issues an annual Invoice to VHS requiring payment of the previous year's
21 accrued contributions in three installments, due on February 15, May 15 and August 15 of the
22 following calendar year. Thus, for 2017 contributions, RPHE issued Invoices to VHS for
23 February 15, 2018 in the amount of \$4,791,218, for May 15, 2018 in the amount of \$4,791,218,
24 and for August 15, 2018 in the amount of \$4,791,217, VHS paid the February 15 and May 15
25 Invoices, but did not pay the Invoice for August 15.

26 4. At my direction and request, the actuaries for RPHE, Willis Towers Watson,
27 prepared an Estimated Funding Contributions for Plan Year 2018 for Verity Health System, a true
28 and correct copy of which is attached hereto as Exhibit A. Exhibit A was prepared by the

1 actuaries ahead of when it is ordinarily prepared, and is an estimate as indicated in the notes to
2 Exhibit A.

3 I declare under penalty of perjury under the laws of the United States of America that the
4 foregoing is true and correct. Executed at Phoenix, Arizona on September 19, 2018.
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8 Michael Holdsworth

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Trodeila & Lapping LLP
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San Francisco, CA 94133

Estimated Funding Contributions for Plan Year 2018

Verity Health System

1. Costs incurred between January 1, 2018 through August 31, 2018

a. Normal Cost	2,738,677
b. Expected Administrative Expenses	419,537
c. Interest	142,120
d. Subtotal [1.a. + 1.b. + 1.c.]	3,300,334

2. Costs incurred between September 1, 2018 through December 31, 2018

a. Normal Cost	1,369,339
b. Expected Administrative Expenses	209,769
c. Interest	177,649
d. Subtotal [2.a. + 2.b. + 2.c.]	1,756,757

3. Amortization of Prior Obligations

a. Amortization of Unfunded Actuarial Accrued Liability	
(i) Actuarial Accrued Liability	401,839,352
(ii) Actuarial Value of Assets	339,789,122
(iii) Unfunded Actuarial Accrued Liability [3.a.(i) - 3.a.(ii)]	62,050,230
(iv) Ten-year amortization of 3.a.(iii)	8,732,739
b. Amortization of the Withdrawn Employer Surplus Credit	
(i) Withdrawn Employer (Surplus) / Deficit	(26,436,289)
(ii) Ten-year amortization of 3.b.(i)	(3,720,554)
(iii) Verity Health's portion of Actuarial Value of Assets	29.60%
(iv) Verity's Withdrawn Employer Surplus Credit [3.b.(ii) x 3.b.(iii)]	(1,101,156)

3. Estimated 2018 Funding Contribution [1.d. + 2.d. + 3.a.(iv) + 3.b.(iv)] 12,688,674

Notes

- Estimates based on the data, provisions and assumptions outlined in the August 16, 2018 materials for the Board of Trustees meeting. Final results will vary due to:
 - a. Actual demographic experience in 2017 different than assumed
 - b. Audited assets being different than unaudited amounts
 - c. Contributions for the 2017 plan year being different than expected
- Estimates were calculated at a 6.75% valuation interest rate
- Amounts shown herein do not include any assessments for extraordinary administrative expenses, which may be assessed to individual employers at the Board's discretion, except for the \$25,000 annual cost to administer Verity cash balance formula for CNA nurses

EXHIBIT A