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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.	Chapter 11 Lead Case No. 2:18-bk-20151-ER Hon. Ernest M. Robles Adv. Proc. No. __-_____
OFFICIAL COMMITTEE OF UNSECURED CREDITORS of VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al*., Plaintiff, v. U.S. BANK NATIONAL ASSOCIATION, as trustee, Defendant.	**COMPLAINT FOR DETERMINATION OF VALIDITY, PRIORITY, AND EXTENT OF LIENS AND SECURITY INTERESTS** Hearing to be scheduled.

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The Official Committee of Unsecured Creditors ("Plaintiff" or the "Committee") of debtors and debtors-in-possession (collectively, the "Debtors") in the above-captioned chapter 11 cases, for and on behalf of the Debtors' estates, as and for its adversary complaint (the "Complaint"), against Defendant U.S. Bank National Association in its capacity as trustee ("Defendant" and together with Plaintiff, the "Parties"), pursuant to Federal Rule of Bankruptcy Procedure 7001 and title 11 of the United States Code, 11 U.S.C. §§ 101 et seq. (the "Bankruptcy Code"), hereby respectfully alleges as follows:

NATURE OF THE ACTION

1. This is an adversary proceeding brought pursuant to, *inter alia*, Federal Rule of Bankruptcy Procedure 7001, sections 105 and 502 of the Bankruptcy Code, and other applicable law, seeking a declaratory judgment determining the validity, priority, and extent of the liens against property of the Debtors' estates held by Defendant.

2. The Committee seeks a determination that other than the property identified in Exhibit A (the "Collateral"), as of the Petition Date, Defendant does not have a perfected security interest in any of the Debtors' assets—and, in particular, Defendant does not have a perfected security interest in the deposit accounts of the Debtors set forth in Section I of Exhibit B hereto (the "Deposit Accounts") or the funds therein, or in the entities or the assets of the entities set forth in Section II of Exhibit B hereto, nor does Defendant have any rights and/or interests in any so-called quality assurance fee ("QAF") revenue funds arising under California Welfare & Institutions Code sections 14169.54 and 14169.55, or the right to any future disbursements on account thereof, relating to QAF periods 7–10 ("Future QAF Reimbursements").

3. Plaintiff has standing to prosecute this Complaint by virtue of, *inter alia*, paragraph 5(e) of 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* (the "Final DIP Order") [Docket No. 409] entered by the Court on October 4, 2018.

4. Paragraph 5(e) of the Final DIP Order provides, in pertinent part:

> (e) **Validity, Perfection and Amount of Prepetition Liens**. The Debtors further acknowledge and agree that, as of the Petition Date, (a) the Prepetition Liens securing the Prepetition Secured Obligations on the Prepetition Collateral and the VMF Liens on the VMF Collateral were valid, binding, enforceable, non-avoidable, and properly perfected and were granted to, or for the benefit of, the Prepetition Secured Creditors and McKesson, (b) the Prepetition Liens were senior in priority over any and all other Liens on the Prepetition Collateral except the prepetition tax lien arising in connection with the CSCDA Special Assessments, and (c) the VMF Liens were senior in priority over any and all other Liens on VMF Collateral. 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) (emphasis added).

5. The Parties have extended the Challenge Deadline on several occasions. As of the date of this filing, the Challenge Deadline is June 13, 2019.

JURISDICTION AND VENUE

6. This Court has jurisdiction over this adversary proceeding by virtue of 28 U.S.C. § 1334(b) and pursuant to 28 U.S.C. § 157(a).

7. This adversary proceeding is a "core" proceeding as defined in 28 U.S.C. §§ 157(b)(2)(A) and (K).

8. In the event that any part of this adversary proceeding is found to be "non-core," Plaintiff consents to the entry of final orders and judgments by this Court, pursuant to Rule 7008 of the Federal Rules of Bankruptcy Procedure.

9. Venue in this District is properly laid pursuant to 28 U.S.C. § 1409.

PARTIES

10. The Committee was formed on September 14, 2018 and was duly appointed on September 17, 2018 by the Office of the United States Trustee pursuant to Section 1102(a)(1) of the Bankruptcy Code [Docket No. 197].

11. The Committee brings this proceeding on behalf of and for the benefit of the Debtors' chapter 11 estates.

12. Upon information and belief, Defendant is a party to the Indentures described in paragraph 21 below. Upon information and belief, Defendant conducts operations in the United States.

RELEVANT FACTS

13. On August 31, 2018 (the "Petition Date"), the above-referenced Debtors filed voluntary cases (the "Bankruptcy Cases") under chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Central District of California.

14. The Debtors are in the business of operating hospitals and other healthcare facilities in California.

15. The Debtors continue in the management and operation of their businesses and properties as debtors-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code. No trustee or examiner has been appointed in the Bankruptcy Cases.

16. On the Petition Date, the Debtors filed their *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* [Docket No. 31] (the "DIP Motion").

17. Pursuant to the Loan Agreements (defined in paragraph 21 below), the Debtors were loaned bond proceeds from the Indentures (referred to in paragraph 21 below) pursuant to which Defendant served as note trustee and collateral agent prior to the Petition Date.

18. This action is to determine the validity, priority, and extent of Defendant's liens and security interests. This action is not brought against Defendant in its individual capacity, but rather solely as a note trustee and collateral agent. Plaintiff does not contend that Defendant has done anything improper.

19. Subject to the limitations set forth, *inter alia*, in paragraph 5(e) of the Final DIP Order, the Debtors stipulated to, *inter alia*, the validity, perfection, and enforceability of Defendant's liens and scope of Defendant's collateral, and waived all rights to challenge such liens. *See* Final DIP Order, ¶ 5(e).

20. Pursuant to paragraph 5(e) of the Final DIP Order, the stipulations and admissions contained in the Final DIP Order are deemed binding upon the Debtors and all non-debtor parties-in-interest, including without limitation the Committee, for all purposes, including, without limitation the validity, perfection, and enforceability of the Prepetition Liens and the Prepetition Secured Obligations (as defined in the Final DIP Order), unless and except to the extent the Committee has initiated a timely Challenge Proceeding (as defined in the Final DIP Order). *See* Final DIP Order, ¶ 5(e).

21. The applicable Debtors' obligations owing to the Defendant are secured by a lien on and security interest in the Collateral pursuant to:

(i) the loan agreements identified in items (1) – (6) below (collectively, the "Loan Agreements"):

(1) Loan Agreement dated as of December 1, 2015 between the California Public Finance Authority and Verity Health System of California, Inc. executed in connection with the $60,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 2015A, as amended by the Amendment to the Loan Agreement dated as of March 2, 2016.

(2) Loan Agreement dated as of December 1, 2015 between the California Public Finance Authority and Verity Health System of California, Inc. executed in

connection with the $45,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 2015B, as amended by the Amendment to the Loan Agreement dated as of March 2, 2016.

(3) Loan Agreement dated as of December 1, 2015 between the California Public Finance Authority and Verity Health System of California, Inc. executed in connection with the $10,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 2015C (FEDERALLY TAXABLE), as amended by the Amendment to the Loan Agreement dated as of March 2, 2016.

(4) Loan Agreement dated as of December 1, 2015 between the California Public Finance Authority and Verity Health System of California, Inc. executed in connection with the $45,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 20l5D, as amended by the Amendment to the Loan Agreement dated as of March 2, 2016.

(5) Loan Agreement dated as of September 1, 2017 between the California Public Finance Authority and Verity Health System of California, Inc. executed in connection with the $21,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 2017.

(6) Loan Agreement dated as of December 1, 2017 between the California Public Finance Authority and Verity Health System of California, Inc. executed in connection with the $21,000,000 California Public Finance Authority Revenue Notes (Verity Health System) Series 2017B.

(ii) the Notes, Indentures (as defined in the Loan Agreements), and Master Indenture (in each case referred to in the applicable Loan Agreement), and

(iii) each Deed of Trust With Fixture Filing and Security Agreement and Assignment of Leases and Rents entered into in connection with the Loan Agreements (individually or collectively, "Deed of Trust").

22. Other than the Collateral, as of the Petition Date, the Defendant does not have a perfected security interest in any of the Debtors' assets, including (i) the Deposit Accounts set forth

in Section I of Exhibit B hereto, (ii) the entities or the assets of the entities set forth in Section II of Exhibit B hereto, (iii) any Future QAF Disbursements, and (iv) any commercial causes of action.

23. A determination by the Court pursuant to Federal Rules of Bankruptcy Procedure 7001(2) and 7001(9), sections 105 and 502 of the Bankruptcy Code, and other applicable law regarding the validity, priority, and extent of Defendant's liens against the Debtors' estates is necessary to the proper administration of the Debtors' estates.

24. All rights to bring avoidance or similar actions under Chapter 5 of the Bankruptcy Code or similar state law (collectively, "Avoidance Actions") are reserved. Nothing in this Complaint shall be considered to be a waiver of any rights of the Committee, the Debtors, a liquidating trust, or any other entity with standing, to bring Avoidance Actions against any party.

FIRST CLAIM FOR RELIEF

(Declaratory Relief – Clarification of Final DIP Order)

25. The Committee restates and re-alleges each of the foregoing allegations as if fully set forth herein.

26. Paragraph 5(e) of the Final DIP Order provides that "the Prepetition Liens securing the Prepetition Secured Obligations on the Prepetition Collateral and the VMF Liens on the VMF Collateral were valid, binding, enforceable, non-avoidable, and properly perfected and were granted to, or for the benefit of, the Prepetition Secured Creditors and McKesson."

27. Read literally, paragraph 5(e) of the Final DIP Order mistakenly suggests that Defendant has a perfected security interest in all of the assets of all of the Debtors.

28. As of the Petition Date, Defendant does not have a perfected security interest in *all* of the assets of all of the Debtors, but rather only in the Collateral set forth on Exhibit A. Defendant does not have a perfected security interest in any of the Debtors' other assets, including (i) the Deposit Accounts set forth in Section I of Exhibit B hereto, (ii) the entities or the assets of the entities set forth in Section II of Exhibit B hereto, (iii) any Future QAF Disbursements, and (iv) any commercial causes of action.

SECOND CLAIM FOR RELIEF

(Declaratory Relief – Deposit Accounts And Entities)

29. The Committee restates and re-alleges each of the foregoing allegations as if fully set forth herein.

30. Defendant does not have a perfected security interest in the Deposit Accounts set forth in Section I of Exhibit B hereto because (a) there are no deposit account control agreements for the Deposit Accounts, (b) there is no possession of the funds in the Deposit Accounts by Defendant, and (c) the funds in the Deposit Accounts do not constitute identifiable cash proceeds of an otherwise perfected, unavoidable lien in other collateral of the Defendant.

31. Defendant does not have a perfected security interest in the entities or the assets of the entities set forth in Section II of Exhibit B hereto.

THIRD CLAIM FOR RELIEF

(Declaratory Relief – Future QAF Disbursements)

32. The Committee restates and re-alleges each of the foregoing allegations as if fully set forth herein.

33. Defendant does not have a perfected security interest in Future QAF Disbursements because, among other things, (a) Future QAF Disbursements do not constitute proceeds of pre-petition collateral, (b) the value of a lien in Future QAF Disbursements to Defendant is $0.00 given that, as of the Petition Date, Defendant could not foreclose on its purported security interest and demand collection from the State of California, (c) the value of Future QAF Disbursement to Debtors on the Petition Date was $0.00 because Debtors had not undertaken the commitments or satisfied the conditions precedent to have any rights to Future QAF Disbursements, and/or (d) Future QAF Disbursements depended completely upon post-petition services of the Debtors.

34. Accordingly, any purported lien in any Future QAF Disbursements in favor of Defendant must be avoided.

PRAYER FOR RELIEF

WHEREFORE, the Committee respectfully requests that the Court:

(a) issue a declaratory judgment that, notwithstanding the language of Paragraph 5(e) of the Final DIP Order, as of the Petition Date Defendant does not have a perfected security interest in any of the Debtors' assets other than the Collateral set forth on Exhibit A hereto;

(b) issue a declaratory judgment that Defendant does not have a perfected security interest in (i) the Deposit Accounts set forth in Section I of Exhibit B hereto, or (ii) the entities or the assets of the entities set forth in Section II of Exhibit B hereto;

(c) issue a declaratory judgment that Defendant does not have a perfected security interest in Future QAF Disbursements; and

(d) grant any further relief as the Court deems just and proper.

DATED: June 13, 2019

MILBANK LLP

/s/ Mark Shinderman
Mark Shinderman
Robert J. Liubicic
Alexandra Achamallah

ARENT FOX LLP
Thomas E. Jeffry Jr.
Robert M. Hirsh (admitted *pro hac vice*)

Counsel for the Official Committee of Unsecured Creditors of Verity Health System of California, Inc., et al.

Exhibit A

Defendant is secured by a lien on and security interest in the following property:

(1) Real Property:

Property Address	APN
3630 E. Imperial Highway Lynwood, CA 90262	6173-021-008, 007, 006
2700 E. Slauson Ave., Huntington Park, CA 90255	6320-006-069
5957/5931 Atlantic Blvd., Maywood, CA 90270	6313-013-026, 028
9340/9400 No Name Uno, Gilroy, CA 95020	835-05-031, 032
600 Marine Blvd., Moss Beach, CA 94038	037-160-090-9

(2) a perfected security interest in the following personal property of Seton Medical Center, Saint Louise Regional Hospital, St. Francis Medical Center, O'Connor Hospital, St. Vincent Medical Center and Seton Coastside (collectively, the "Relevant Debtors") to the extent such property under California law may be perfected by the filing of a financing statement:

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

(b) the accounts listed below; and

(c) to the extent not covered by the foregoing, all products, Proceeds (as defined in the Security Agreements referred to in the Loan Agreements) and replacements of the foregoing;

Company	Financial Institution	Account Number
O'Connor Hospital	Bank of America	XXXXXX3900
St. Louise Regional Hospital	Bank of America	XXXXXX3905
St. Francis Medical Center	Bank of America	XXXXXX3924
St. Vincent Medical Center	Bank of America	XXXXXX3929
Seton Coastside	Bank of America	XXXXXX3887
Seton Medical Center	Bank of America	XXXXXX3882

(3) to the extent not covered by subparagraph (1) or (2) above, with respect to the Relevant Debtors, a perfected security interest in the Property (as defined in the Deed of Trust) of such Relevant Debtors, which under California law may be perfected by the recording of the Deed of Trust in the applicable recording office; and

(4) to the extent not covered by subparagraph (1), (2), or (3) above, with respect to St. Francis Medical Center, St. Louise Regional Hospital, and Verity Holdings LLC, a perfected security interest in the Property (as defined in the Deed of Trust) and/or Personal Property (as defined in the Deed of Trust) of such entities described in the financing statements filed with the California Secretary of State in respect thereof, in each case to the extent such Property and/or Personal Property may be perfected under California law by the filing of a financing statement.

Exhibit B

Exhibit B—Section I

Company	Financial Institution	Account Number
Verity Health System of CA Inc.	Bank of America	XXXXXX6440
Verity Health System of CA Inc.	Bank of America	XXXXXX9250
Verity Health System of CA Inc.	Bank of America	XXXXXX1785
Verity Health System of CA Inc.	Bank of America	XXXXXX2889
O'Connor Hospital	Bank of America	XXXXXX2945
O'Connor Hospital	Bank of America	XXXXXX6389
O'Connor Hospital	Bank of America	XXXXXX3007
O'Connor Hospital	Bank of America	XXXXXX2284
O'Connor Hospital	Bank of America	XXXXXX2662
St. Louise Regional Hospital	Bank of America	XXXXXX2926
St. Louise Regional Hospital	Bank of America	XXXXXX6421
St. Louise Regional Hospital	Bank of America	XXXXXX7575
St. Louise Regional Hospital	Bank of America	XXXXXX2307
St. Francis Medical Center	Bank of America	XXXXXX2940
St. Francis Medical Center	Bank of America	XXXXXX6407
St. Francis Medical Center	Bank of America	XXXXXX3012
St. Francis Medical Center	Bank of America	XXXXXX2487
St. Francis Medical Center	Bank of America	XXXXXX1057
St. Francis Medical Center	Bank of America	XXXXXX1371
St. Francis Medical Center	Bank of America	XXXXXX1357
St. Francis Medical Center	Bank of America	XXXXXX1845
St. Francis Medical Center	Bank of America	XXXXXX1840
St. Francis Medical Center	U.S. Bank	XXXXXX2162
St. Vincent Medical Center	Bank of America	XXXXXX2964
St. Vincent Medical Center	Bank of America	XXXXXX6426
St. Vincent Medical Center	Bank of America	XXXXXX3017
St. Vincent Medical Center	Bank of America	XXXXXX2062
St. Vincent Medical Center	Bank of America	XXXXXX0553
St. Vincent Medical Center	Bank of America	XXXXXX3695
St. Vincent Medical Center	Bank of America	XXXXXX0989
Seton Medical Center	Bank of America	XXXXXX2902
Seton Medical Center	Bank of America	XXXXXX6365
Seton Medical Center	Bank of America	XXXXXX3001
Seton Medical Center	Bank of America	XXXXXX2289
Seton Medical Center	Bank of America	XXXXX02907
Seton Medical Center	Bank of America	XXXXXX6384

Company	Financial Institution	Account Number
Seton Medical Center	Bank of America	XXXXXX2302
Seton Medical Center	Bank of America	XXXXX12907
O'Connor Hospital Foundation	Bank of America	XXXXXX3433
O'Connor Hospital Foundation	Morgan Stanley	XXXXX2-037
St. Louise Regional Hospital Foundation	Bank of America	XXXXXX2521
St. Francis Medical Center Foundation	Bank of America	XXXXXX2809
St. Vincent Medical Center Foundation	Bank of America	XXXXXX3025
St. Vincent Medical Center Foundation	East West Bank	XXXXXX1162
St. Vincent Dialysis Center	Bank of America	XXXXXX8921
Seton Medical Center Foundation	Bank of America	XXXXXX2260
Healy, James T/U/A	Wells Fargo	XXXXXX0089
Verity Business Services	Bank of America	XXXXXX6402
Verity Business Services	Bank of America	XXXXXX2982
Verity Business Services	Bank of America	XXXXXX3192
Verity Medical Foundation	Wells Fargo	XXXXXX9996
Verity Medical Foundation	Wells Fargo	XXXXXX0010
Verity Holdings LLC	Bank of America	XXXXXX1597
Verity Holdings LLC	Bank of America	XXXXXX1248
Verity Holdings LLC	Bank of America	XXXXXX1970
Verity Holdings LLC	Bank of America	XXXXXX1975
Seton Medical Center	Tri Counties Bank	XXXXXX3611
Seton Medical Center Foundation	Tri Counties Bank	XXXXXX8521

Exhibit B—Section II

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