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UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

LOS ANGELES DIVISION

In re VERITY HEALTH SYSTEM OF CALIFORNIA, INC. Debtors and Debtors in Possession. OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., ET AL., Plaintiffs, v. UMB BANK, NATIONAL ASSOCIATION, Defendant.	Case No.: 2:18-bk-20151-ER Adv. No.: 2:19-ap-01166-ER **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** [*Re-filing to correct docketing event*] Hearing Date: November 21, 2019 Time: 10:00 a.m. Courtroom: 1568 Judge: Hon. Ernest M. Robles Complaint Filed: June 13, 2019

1820151191002000000000002

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.

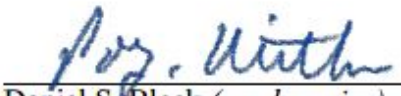
In support of this Motion, UMB relies on the filed pleadings, any documents or facts in the debtors' chapter 11 bankruptcy cases for which the Court may take judicial notice, the accompanying Memorandum of Points and Authorities in Support of Defendant's Motion to Dismiss the Amended Complaint, UMB's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



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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
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- 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*

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UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re

VERITY HEALTH SYSTEM OF CALIFORNIA, INC.

Debtors and Debtors in Possession.

OFFICIAL COMMITTEE OF UNSECURED CREDITORS OF VERITY HEALTH SYSTEM OF CALIFORNIA, INC., ET AL.,

Plaintiffs,

v.

UMB BANK, NATIONAL ASSOCIATION,

Defendant.

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

Adv. No.: 2:19-ap-01166-ER

MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION TO DISMISS THE AMENDED COMPLAINT

[*Re-filing to correct docketing event*]

Hearing
Date: November 21, 2019
Time: 10:00 a.m.
Courtroom: 1568
Judge: Hon. Ernest M. Robles

Complaint Filed: June 13, 2019

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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

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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,

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[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

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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.

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[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.

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[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:

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[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 UMB does not have a lien in the "going concern premium" created in this case 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) 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

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[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.

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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

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[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]

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[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

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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.

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