

UNITED STATES DISTRICT COURT  
CENTRAL DISTRICT OF CALIFORNIA

**CIVIL MINUTES - GENERAL**

Case No. 2:19-cv-00133-RGK Date February 22, 2019

Title *In re Verity Health System of California, Inc.*

Present: The Honorable R. GARY KLAUSNER, UNITED STATES DISTRICT JUDGE

Sharon L. Williams

Not Reported

N/A

Deputy Clerk

Court Reporter / Recorder

Tape No.

Attorneys Present for Plaintiff:

Attorneys Present for Defendant:

Not Present

Not Present

**Proceedings: (IN CHAMBERS) Order Re: California Attorney General's Motion to Stay Pending Appeal (DE 6)**

**I. INTRODUCTION**

On January 7, 2019, appellant Xavier Becerra, the Attorney General of California ("Attorney General"), filed a notice of appeal of the bankruptcy court's order authorizing the sale of debtors' assets, approving the assignment of unexpired related leases, and granting related relief (DE 1). On February 1, 2019, the Attorney General filed the instant emergency motion to stay pending appeal of the bankruptcy court's order authorizing the sale of certain debtors' assets (DE 6). Verity Health System of California, Inc., Official Committee of Unsecured Creditors, and the County of Santa Clara opposed the motion.

For the following reasons, the Court **DENIES** the Attorney General's emergency motion.

**II. FACTUAL BACKGROUND**

On December 3, 2015, the Attorney General consented to the change in governance of Daughters of Charity Health System, now known as Verity Health System of California, Inc. ("Verity"). The Attorney General imposed health and safety protections on each of the five hospitals ("AG Conditions") requiring the hospitals to maintain certain levels of emergency services, intensive care services, cardiac services, and various other services. In addition, the Attorney General contemplated a future sale of the hospitals and provided that the AG Conditions shall be legally binding on the parties to any future transaction.

On August 31, 2018, Verity and certain subsidiaries (collectively, "Debtors") filed a petition for relief under Chapter 11 of the Bankruptcy Code. The same day, the bankruptcy court entered an order granting the Debtors' motion for joint administration of the Debtors' assets. On October 10, 2018, the Attorney General objected to the Debtors' proposal to sell O'Connor Hospital and Saint Louise Regional



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Hospital free and clear of the AG Conditions. The bankruptcy court preserved the objections for the sale hearing.

On October 31, 2018, the bankruptcy court entered an order establishing auction procedures for the sale of the two hospitals. The County of Santa Clara was identified as a stalking horse bidder. The court then set a hearing date of December 19, 2018 to consider the Debtors' motion for the entry of an order approving the sale. The County of Santa Clara's Asset Purchase Agreement ("APA") provides that it is not required to accept a sale order that does not provide for the sale free and clear of all liens, claims, and interests. The bankruptcy court found that this includes the AG Conditions.

On November 2, 2018, the County of Santa Clara asked the Attorney General to clarify his position as to whether the AG Conditions applied to the sale and argued that because the County is a government entity, certain AG Conditions would be impossible to meet without violating California law or the California Constitution. On November 9, 2018, the Attorney General responded that five of the AG Conditions would be waived. Then on December 14, 2018, the Attorney General filed a response to the Debtors' memorandum in support of the sale motion, providing that "[t]he California Attorney General does not object to the sale to the County of Santa Clara, in light of the conditions as clarified in the Attorney General's November 9, 2018 letter . . ." and that "[t]he Attorney General and the County are presently engaged in further discussions about the Conditions not addressed by the Attorney General's November 9, 2018 letter, and as such, the Attorney General will continue to consider any further requests for clarification or modification presented by the County." (AG Appx. No. 8, at 895, ECF No. 8-8A.)

At the sale hearing on December 19, 2018, the Attorney General argued that the December 14, 2018 response was poorly drafted, and that it does object to the sale of the hospitals free and clear of the AG Conditions. The Debtors and the County of Santa Clara argued that the Attorney General had waived its objections and was estopped from asserting them at the hearing.

The bankruptcy court made three findings in its December 26, 2018 decision: 1) the Attorney General waived his right to object to a sale free and clear of the AG Conditions; 2) the Attorney General is equitably estopped from contesting the sale; and 3) a sale of the hospitals free and clear of the AG Conditions is authorized under 11 U.S.C. § 363(f)(1). The bankruptcy court also denied the Attorney General's request for a 14-day stay of the sale order under Bankruptcy Rule 6004(h). On December 27, 2018, the bankruptcy court authorized the sale of the hospitals to the County of Santa Clara free and clear of the AG Conditions.

On January 7, 2019, the Attorney General appealed the sale order to this Court. On January 9, 2019, the Attorney General filed a motion to stay the sale order pending appeal in bankruptcy court. The bankruptcy court denied the motion on January 30, 2019 for four reasons: 1) the Attorney General failed

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to show that his appeal was likely to succeed on the merits; 2) mootness within bankruptcy does not demonstrate irreparable injury; 3) the balance of the hardships strongly favors a sale of the hospitals; and 4) the public interest weighed against a stay because the hospitals would likely close.

On February 1, 2019, the Attorney General filed an emergency motion to stay pending appeal in this Court. The sale is anticipated to occur no earlier than February 28, 2019.

### **III. JUDICIAL STANDARD**

District courts may order a stay of a judgement, order, or decree of a bankruptcy court pending appeal. Fed. R. Bankr. P. 8007. Under the Federal Rule of Bankruptcy (“Rule”) 8007, a motion for stay of a bankruptcy court order pending appeal must first be presented to the bankruptcy court. *Id.* Where the bankruptcy court has denied a stay, the district court determines whether the bankruptcy court abused its discretion. *In re Wymer*, 5 B.R. 802, 807 (9th Cir. BAP 1980); *see also In re Irwin*, 338 B.R. 839, 844 (E.D. Cal. 2006); *Universal Life Church, Inc. v. United States*, 191 B.R. 433, 444 (E.D. Cal. 1995). “A bankruptcy court abuses its discretion if it [1] applies an incorrect legal standard or misapplies the correct legal standard, or [2] if its fact findings are illogical, implausible or not supported by evidence in the record.” *In re City of Stockton, California*, 542 B.R. 261, 272 (9th Cir. BAP 2015). “Ultimately, ‘discretion is abused only where no reasonable man would take the view adopted by the [bankruptcy] court’—stated differently, ‘[i]f reasonable men could differ as to the propriety of the action taken by the [bankruptcy] court, then it cannot be said that the [bankruptcy] court abused its discretion.’” *In re BGM Pasadena, LLC*, 2016 WL 3212243, at \*2 (C.D. Cal. June 2, 2016) (citing *In re Irwin*, 338 B.R. at 844).

An appellant seeking a stay pending appeal under Rule 8007 must show: “(1) movant’s likelihood of success on the merits of the appeal; (2) significant and/or irreparable harm that will come to the movant absent a stay; (3) harm to the adverse party if the stay is granted; and (4) where the public interest lies.” *In re BGM Pasadena, LLC*, 2016 WL 3212243, at \*2; *In re Irwin*, 338 B.R. at 843; *Universal Life Church*, 191 B.R. at 444. The moving party bears the burden of proof on each element. *In re Irwin*, 338 B.R. at 844. Failure to satisfy a single prong “dooms the motion.” *Id.* (citing *In re Deep*, 288 B.R. 27, 30 (N.D.N.Y. 2003)).

### **IV. DISCUSSION**

The Attorney General asks the Court to stay the bankruptcy court’s sale order pending appeal because without the AG Conditions, the hospitals will no longer be required to operate as acute care hospitals, 24-hour emergency rooms, provide women’s health services, and other specific services. The APA does not specify which clinical services will be provided and as such, the Attorney General believes that the County of Santa Clara is refusing to commit to providing the essential healthcare



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services listed in the AG Conditions. Because the sale is expected to close at the end of the month, the Attorney General argues, an emergency stay is necessary.

Three parties oppose the Attorney General's motion. First, Verity argues that the Attorney General lacks the authority to impose conditions on the sale, the Attorney General waived its right to object, and the factors weigh against a stay. The Committee of Unsecured Creditors agrees that the Attorney General has not shown that the bankruptcy court abused its discretion and has failed to provide a meritorious basis for the stay. Finally, the County of Santa Clara also joins the Debtors' opposition.

**A. Whether the Bankruptcy Court Abused its Discretion**

The bankruptcy court did not abuse its discretion when it denied the Attorney General's motion for a stay pending appeal. First, the court applied the correct legal standard. *See In re City of Stockton, California*, 542 B.R. at 272. Second, its findings are not illogical, implausible, or unsupported by the record. *Id.* The four factors weigh against granting a stay. *See In re BGM Pasadena, LLC*, 2016 WL 3212243, at \*2.

*1. Likelihood of Success on the Merits*

First, the Attorney General has failed to show that his appeal is likely to succeed on the merits. "[I]t is not enough that the likelihood of success on the merits is 'better than negligible' or that there is a 'mere possibility of relief.'" *Lair v. Bullock*, 697 F.3d 1200, 1204 (9th Cir. 2012) (citing *Nken v. Holder*, 556 U.S. 418, 434 (2009)). "[A]t a minimum, a petitioner must show that there is a substantial case for relief on the merits." *Id.* (internal citations omitted). But "[t]he standard does not require the petitioners to show that it is more likely than not that they will win on the merits." *Id.*

The bankruptcy court rejected the Attorney General's objections to the sale in part because the Attorney General failed to show that it has the authority to review the sale of the hospitals to the County. Under California Corporations Code § 5914, the sale of a not-for-profit healthcare facility is subject to review by the Attorney General when it is being sold or transferred to a for-profit corporation or entity, or a mutual benefit corporation or entity. Cal. Corp. Code § 5914. But here, as the bankruptcy court explained, the sale is to a *public entity*—the County of Santa Clara. As a result, the sale is not reviewable by the Attorney General under this code section.

The Attorney General also cited California Corporations Code § 5926, which provides that he "may enforce conditions imposed on the Attorney General's consent to an agreement or transaction pursuant to Section 5914 or 5920 to the fullest extent provided by law." Cal. Corp. Code § 5926. But because the bankruptcy court was not persuaded that any other law allowed the Attorney General to enforce the AG Conditions, this section is unavailing.

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In the instant motion, the Attorney General cites to California Government Code § 12598 for the proposition that he is “charged with the supervision and regulation of nonprofit corporations and other charitable trusts in this state.” (Mot. 11:24–26, ECF No. 6.) The Attorney General also cites to his broad police and regulatory powers under California Corporations Code § 5914 and related sections. Finally, the Attorney General argues that the bankruptcy court “was required to apply non-bankruptcy law under Bankruptcy Code sections 959(b)” and “sections 363(d)(1), 541(f), 1129(a)(16), and 1121(d) that specifically provide that applicable non-bankruptcy law applies to sales of assets by a nonprofit debtor.” (*Id.* at 12:10–1.) For example, 28 U.S.C. § 959(b) provides that bankruptcy trustees must comply with state law. 28 U.S.C. § 959(b). Similarly, 11 U.S.C. § 363(d)(1) states that a trustee may only sell property in accordance with applicable non-bankruptcy law. 11 U.S.C. § 363(d)(1). But none of those sections help the Attorney General here, because the bankruptcy court’s opinion did not impermissibly ignore California law; on the contrary, the court found that “the Attorney General did not cite to any provision of California law entitling him to enforce successorship liability under the circumstances of this case.” (AG Appx. 8B-1, at 952, ECF No. 8-11.)

Here, the Attorney General still has not cited to provisions of California law entitling him to enforce the AG Conditions. As a result, the bankruptcy court’s findings are logical and supported by the record. The Attorney General has failed to show a likelihood that he will succeed on the merits of his appeal.<sup>1</sup>

2. *Irreparable Injury*

Similarly, the Attorney General has failed to show that it will suffer irreparable injury in the absence of a stay. The Attorney General contends that because the sale may moot his appeal, he will suffer irreparable injury. “[I]t is well settled that an appeal being rendered moot does not itself constitute irreparable harm.” *In re Gardens Regional Hospital and Medical Center, Inc.*, 567 B.R. 820, 831 (Bankr. C.D. Cal. 2017); *In re BGM Pasadena LLC*, 2016 WL 3212243, at \*8 (citing *In re 203 N. LaSalle St. Pshp.*, 190 B.R. 595, 598 (N.D. Ill. 1995)); *see also In re Irwin*, 338 B.R. at 853; *In re Fullmer*, 323 B.R. 287, 304 (Bankr. D. Nev. 2005) (collecting cases). As a result, the bankruptcy court did not abuse its discretion when it found that the Attorney General failed to show irreparable harm based on the possibility of mootness.

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<sup>1</sup> The bankruptcy court also found that the Attorney General waived his right to object to the sale free and clear of the AG Conditions and that he was equitably estopped from raising the argument now. But the Court does not need to assess the merits of these findings, because absent authority to review the sale in the first place, the Attorney General has no authority to enforce the AG Conditions regardless of whether he waived his objection.

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The Attorney General also argues that the families and patients served by the two hospitals will suffer irreparable injury if the transaction closes because they may lose the essential services safeguarded by the AG Conditions. But the Attorney General has provided no basis for this contention. In contrast, Verity has provided evidence that a stay of the sale order would most likely result in a closure of the hospitals, which in turn would cause delays in healthcare services to the community. (*See, e.g., AG Appx. 16, at 1150, ECF No. 8–14.*) This factor therefore weighs against a stay.

3. *Balance of the Hardships*

Third, the bankruptcy court did not abuse its discretion when it found that the balance of the hardships weighed against a stay. The court found after assessing the testimony of several witnesses that a stay would put the transaction in danger of collapse, which could in turn waste the resources expended in furtherance of the sale and harm employee morale. In comparison, if the absence of a stay, the Attorney General may lose its ability to appeal the decision. The bankruptcy court found that the injury to the Attorney General was less severe. These findings are supported by the evidence. As a result, this factor weighs against a stay.

4. *Public Interest Factors*

Finally, the public interest factors weigh against a stay. As discussed, a stay may result in the cancellation of the sale, which could in turn lead to a closure of both hospitals. The bankruptcy did not abuse its discretion when it found that “[f]ar from protecting public health and welfare, a stay would set in motion a series of events that, in all probability, would reduce the availability of healthcare services to the public.” (Verity Appx. 11, at 332, ECF No. 16-5.)

5. *Conclusion*

The Attorney General has failed to show that the factors weigh in favor of a stay. Accordingly, the district court did not abuse its discretion when it denied the Attorney General’s request for a stay.

**V. CONCLUSION**

For the foregoing reasons, the Court **DENIES** the Attorney General’s emergency motion.

**IT IS SO ORDERED.**

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