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UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA
LOS ANGELES DIVISION

In re: VERITY HEALTH SYSTEM OF CALIFORNIA, INC., *et al.*,

Debtors and Debtors In Possession

STRATEGIC GLOBAL MANAGEMENT, INC.[1]

Appellant

v.

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

Appellees

District Court Case No.:
2:19-cv-10352-DSF

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

Hon. Dale S. Fischer

DEBTORS' RESPONSE TO STRATEGIC GLOBAL MANAGEMENT, INC.'S MOTION FOR ORDER DIRECTING THE PARTIES TO: (1) COMPLY WITH GENERAL ORDER NO. 11-10, § 5, AND DISTRICT COURT LOCAL RULE 16-15; AND (2) PARTICIPATE IN ADR PROCESS

Date: [TBD]
Time: [TBD]
Courtroom: 7D
Location: 350 W. First Street
Los Angeles, CA 90012

[1] The other Debtors in the chapter 11 cases, jointly administered under Lead Case No. 2:18-bk-20151-ER, are O'Connor Hospital 2:18-bk-20168-ER, Saint Louise Regional Hospital 2:18-bk-20162-ER, St. Francis Medical Center 2:18-cv-20165-ER, St. Vincent Medical Center 2:18-bk-20164-ER, Seton Medical Center 2:18-cv-20167-ER, O'Connor Hospital Foundation 2:18-bk-20179-ER, Saint Louise Regional Hospital Foundation 2:18-cv-20172-ER, St. Francis Medical Center of Lynwood Foundation 2:18-cv-20178-ER, St. Vincent Foundation 2:18-cv-20180-ER, St. Vincent Dialysis Center, Inc. 2:18-cv-20171- ER Seton Medical Center Foundation 12:8-cv-20175-ER, Verity Business Services 2:18-cv-20173-ER, Verity Medical Foundation 2:18-cv-20169-ER, Verity Holdings, LLC 2:18-cv-20163-ER, DePaul Ventures, LLC 2:18-cv-20176-ER, and DePaul Ventures - San Jose Dialysis, LLC 2:18-cv-20181-ER.

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Verity Health System of California, Inc. ("VHS"), and the above-referenced affiliated debtors and debtors-in-possession (the "Debtors") in the above-captioned chapter 11 cases (the "Bankruptcy Cases") pending in the United States Bankruptcy Court for the Central District of California (the "Bankruptcy Court") and the appellees herein, hereby submit this opposition (the "Opposition") to the *Motion for Order Directing Parties To (1) Comply With General Order No. 11-10, § 5, And District Local Rule 16-15; And (2) Participate In ADR Process* (the "Motion"), filed by appellant, Strategic Global Management, Inc. ("SGM") on January 8, 2020 in each of the three related appeals[2] currently pending before this Court (the "Appeals"). This Opposition is based on the appendix [Docket No. 3] (the "Debtors' Appendix") previously filed in this appeal, the *Declaration of Tania M. Moyron* (the "Moyron Declaration") attached hereto, and the *Request for Judicial Notice* (the "RJN") filed concurrently herewith.

I. INTRODUCTION

SGM has moved the Court for an order compelling the parties to participate in mediation. The Debtors object to the request as mediating the parties' dispute is not appropriate at this point in time and would not be productive. Such a mediation would only distract from the Debtors' priority, which is protecting patient care and saving the Debtors' remaining hospitals given that SGM chose not close the sale of four of the Debtors' hospitals (collectively, the "Hospitals"), despite several orders entered by the Bankruptcy Court. As a consequence of SGM's conduct, the Debtors, among other things, have already been forced to close one Hospital—St. Vincent Medical Center ("SVMC")—and lost tens of millions of dollars.

By way of background, SGM wrongfully induced the Debtors to enter an Asset Purchase Agreement ("APA") for the sale of the Hospitals under the auspices of a

[2] The Appeals are Case Nos. 2:19-cv-10352-DSF, 2:19-cv-10354-DSF, 2:19-cv-10356-DSF.

Bankruptcy Court order, with which SGM had no intention of complying. The Debtors expended tremendous human resources, time and effort with respect to the sale, while incurring significant additional expense performing under the APA and diligently preparing for a closing of the sale for nearly a year. During that time, the Debtors suffered sustain daily operating losses of $450,000. Once all contingencies precedent to close under the APA were satisfied, waived or passed, SGM repeatedly defaulted under the APA and refused to close the sale, levied factually meritless and legally irrelevant accusations against the Debtors, and sought to coerce the Debtors into a re-trade at a substantially lower purchase price. Along the way, SGM violated the Bankruptcy Court's orders providing that SGM was obligated to close the sale. SGM's conduct was calculated, intentional, fraudulent and callous, designed to take advantage of the Debtors' good faith desire to ensure that the hospitals were sold to a purchaser who would keep them open, in order to continue providing critical access to health care in low income communities and jobs to thousands of employees.

The Debtors terminated the APA effective December 27, 2019, because SGM defaulted under the APA and failed to close the sale transaction by December 5, 2019. On January 9, 2020, the Bankruptcy Court granted the Debtors' emergency motion to close SVMC, one of the Hospitals that SGM had agreed to purchase under the APA. The limited resources of the Debtors and their advisors must remain devoted to that process, given the estimated daily operating losses of approximately $450,000 being shouldered by the Hospitals. Mediation at this time would distract from those efforts.

In addition, on January 3, 2020, the Debtors filed a complaint against SGM and its alter egos, seeking damages for their breach of the APA and related torts, which commenced Adversary Proceeding No. 2:20-ap-01001-ER (the "Adversary Proceeding"). The summons and complaint (the "Complaint") in that action were served this week. The complexity of these Appeals, the related Adversary

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Proceeding, and the Bankruptcy Cases, undercut the notion that the Alternative Dispute Resolution process—one that SGM recognizes is developed for "civil litigation"[3]—would best-serve the parties at this time. *See* Mot. at 10 (quoting Local Rules, Chapter I, Rule 16-15.1); *see also* Gen. Order 11-10, § 5.1 (pertaining to "all civil cases").

The Debtors may be willing to participate in mediation once they have conducted preliminary discovery. At this time, however, the parties are not positioned to have meaningful settlement discussions without the benefit of discovery concerning the Debtors' claims. Accordingly, the Debtors respectfully request that SGM's Motion be denied.

II. BACKGROUND

A. The Bankruptcy Proceeding

1. On August 31, 2018 (the "Petition Date"), the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code. *See* Debtors' App. at 3.

2. On the Petition Date, Debtor VHS, a California nonprofit public benefit corporation, was the sole corporate member of five Debtor California nonprofit public benefit corporations that operated O'Connor Hospital and Saint Louise Regional Hospital, and currently operates St. Francis Medical Center and Seton Medical Center, including Seton Medical Center Coastside Campus. *Id*. at 4. As discussed below, the Debtors are in the process of closing SVMC.

[3] Notably, the Court's Local Rules Governing Bankruptcy Appeals, Cases, and Proceedings do not contain an Alternative Dispute Resolution provision nor do they incorporate Local Civil Rule 16-15. *See* Local Rules, Chapter IV, Rule 1 ("Unless the Federal Rules of Bankruptcy Procedure or these Local Rules state otherwise, the Federal Rules of Appellate Procedure, the Federal Rules of Civil Procedure, the Federal Rules of Evidence, and the Ninth Circuit Rules shall apply.").

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B. The Sale and AG Conditions

3. On May 2, 2019, the Bankruptcy Court entered an order approving the sale (the "Sale") of the Hospitals to SGM pursuant to the terms of the APA. *Id.* at 853. The Sale was one of the central objectives of the Debtors' Bankruptcy Cases, and was intended to preserve patient care in the Hospitals' communities, protect over 4,000 jobs, allow physician and trade creditors to maintain going-forward business relationships, and presented the most likely source of recovery to unsecured creditors.

4. On September 25, 2019, the California Attorney General (the "AG") consented to the Sale subject to certain conditions, some of which were materially different than those SGM developed and contractually agreed to in Schedule 8.6 of the APA (the "Additional Conditions"). *Id.* at 991-1030.

5. On September 30, 2019, the Debtors filed a motion (the "Enforcement Motion"), which sought (i) entry of an order enforcing the Sale Order, (ii) a finding that the Sale was free and clear of the Additional Conditions, and (iii) a finding limiting the Sale to only those conditions to which SGM contractually agreed to assume in Schedule 8.6 of the APA. *Id.* at 870. On October 10, 2019, SGM filed a statement in support of the Enforcement Motion expressly requesting that the Bankruptcy Court enter an order granting the Enforcement Motion. *Id.* at 1157

6. On October 23, 2019, the Court entered a memorandum of decision (the "Enforcement Memo Decision") granting the Enforcement Motion. *Id.* at 1165.

C. The Enforcement Order and 8.6 Order

7. After the Bankruptcy Court entered the Enforcement Memo Decision, the AG, the Debtors, and SGM engaged in discussions concerning a proposed form of order. *Id.* at 1199. While the Debtors and the AG agreed to specific language (the "Proposed Order"), despite best efforts, the Debtors were unable to obtain SGM's agreement. On November 8, 2019, the Debtors and the AG filed a stipulation (the "Stipulation") and lodged the Proposed Order. *Id.* at 1189, 1197, 1204. Pursuant to

the Stipulation, (i) the AG agreed to the Proposed Order authorizing the Sale free and clear of "Additional Conditions," (ii) the Debtors agreed to obtain a withdrawal of the Enforcement Memo Decision, and (iii) the AG agreed not to appeal the Proposed Order. *Id.* at 1191.

8. On November 11, 2019, SGM filed an objection to the Proposed Order (the "SGM Objection") and lodged a competing order. *Id.* at 1208, 1228. On November 13, 2019, the Bankruptcy Court held a hearing, heard arguments, and overruled the SGM Objection. *Id.* at 1252.

9. On November 14, 2019, the Bankruptcy Court entered the Enforcement Order granting the Enforcement Motion. *Id.* at 1318. The Enforcement Order found that the "Assets (as defined in the APA) are being sold free and clear of the Additional Conditions without the imposition of any other conditions which would adversely affect the Purchaser (as defined in the APA)," which were the express findings required by Section 8.6 of the APA. *Id.* at 1319. On November 29, 2019, SGM appealed the Enforcement Order. *Id.* at 1321. That appeal is currently pending before the Court under Case No. 19-10352-DSF.

10. On November 18, 2019, the Bankruptcy Court entered an Order finding that SGM was obligated to promptly close the sale under §8.6 of the APA (the "8.6 Order"). *See id.* at 1158. The 8.6 Order provides, in relevant part, that:

> The Debtors have complied with their obligation under the APA to obtain a final, non-appealable Supplemental Sale Order. Consequently, SGM is now obligated to promptly close the SGM Sale, provided that all other conditions to closing have been satisfied.

Id. at 1354.

11. In conjunction with the 8.6 Order, the Bankruptcy Court entered a memorandum of decision, wherein the Court found, among other things, that "SGM is judicially estopped from contending that it is entitled to the Evaluation Period and

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is not obligated to promptly close the sale." *Id.* at 1351. On November 29, 2019, SGM appealed the 8.6 Order. *Id.* at 1355.

D. The Status Conference and Closing Order

12. On November 27, 2019, after briefing and a hearing, the Bankruptcy Court entered an Order finding SGM was obligated to close the Sale by no later than December 5, 2019 (the "Closing Order"). Debtors' App. at 1373.

13. The Bankruptcy Court issued a memorandum of decision supporting the Closing Order, wherein the Court found that "[t]he Court has previously found that the conditions precedent to closing set forth in [Section] 8.6 of the APA has been satisfied. All other conditions precedent to closing were satisfied as of November 19, 2019." *Id.* at 1371. Pursuant to the APA, SGM was required to close the Sale within 10 business days of the Debtors' satisfaction of all conditions to closing. *Id.* On December 3, 2019, SGM appealed the Closing Order. *Id.* at 1375.

E. APA Termination, Plan B, and the Adversary Proceeding

14. On December 6, 2019, the Debtors filed a motion requesting, among other things, entry of an order to show cause why SGM failed to close the Sale on December 5, 2019. *See* RJN Ex. A. On December 9, 2019, the Bankruptcy Court entered an order and memorandum of decision denying the motion and providing that:

> [a]ny efforts undertaken by the Debtors with respect to the alternative disposition of the Hospitals will not violate the Debtors' obligation under Article 12.1 of the APA to cooperate with SGM to consummate the SGM Sale; nor shall any such efforts constitute a material default by the Debtors under any other provision of the APA.

Id. Exs. B, C. On December 17, 2019, the Debtors sent SGM a letter declaring SGM in material breach of the APA and providing notice that the APA would terminate

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effective December 27, 2019. *See id.* Ex. D. The APA terminated effective December 27, 2019. *See id*.

15. On January 3, 2020, the Debtors filed the Complaint against SGM and its alter egos. The Complaint asserts claims arising from SGM's conduct with respect to the APA and the Sale, including breach of contract, promissory fraud, and tortious breach of contract based on the defendants' breaches of the implied covenant of good faith and fair dealing. *See* RJN Ex. E. On January 13, 2020, the Debtors served the Complaint on the defendants, including SGM. *See* Moyron Decl. ¶ 3.

16. As set forth in the Debtors' motion to dismiss this Appeal, the Debtors have daily operational losses of $450,000. *See* Docket No. 2 (Adcock Decl. ¶ 7). On January 6, 2020, the Debtors filed a motion to close SVMC based on, among other things, SVMC's continuing economic losses and the Debtors' need to have sufficient cash on hand for the orderly closure of SVMC. *See* RJN Ex. F. On January 9, 2020, the Bankruptcy Court entered an order and memorandum of decision granting the motion and authorizing the closure of SVMC. *See id.* Exs. G, H. As of the date of this Opposition, the Debtors are in the process of closing SVMC on an expedited basis in the interest of patient safety. *See* Moyron Decl. ¶ 4.

III. ARGUMENT

Mediation at this time would be premature and unproductive. The Debtors appreciate the importance of Alternative Dispute Resolution and anticipate that mediation may be useful for the parties at some point in the future.

As explained above, the Debtors had anticipated that the Sale transaction would timely close before December 31, 2019, which would have put an end to the Debtors' daily operating losses of $450,000. Because SGM failed to close the Sale, however, the Debtors have been forced to devote available resources to stabilizing operations at the Hospitals and pursuing alternatives for each of the Hospitals, including an expedited and smooth closure of one of the Hospitals (SVMC) to protect

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patient care. That process began just last week pursuant to the Bankruptcy Court's order. A mediation in the near term would distract from these critical efforts, which appropriately are consuming the full attention of the Debtors and their counsel.

No decision in this appeal will resurrect the APA, or have any impact on the sale and disposition of the Hospitals.

Finally, the parties' dispute is much larger than the narrow issue presented in this appeal. The Complaint asserts substantial damage claims against SGM and its alter egos. Discovery in that action will be extensive and will play a central role in moving the parties to a place where mediation might be productive. Unless and until that discovery takes place, any mediation of the narrow issue presented in this appeal will be premature and unproductive.

IV. CONCLUSION

For the foregoing reasons, the Debtors respectfully request that the Court deny the Motion.

Dated: January 15, 2020

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By: */s/ Tania M. Moyron*
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DECLARATION OF TANIA MOYRON

I, Tania M. Moyron, submit this Declaration in support of the *Debtors' Response to Strategic Global Management, Inc.'s Motion for Order Directing the Parties to: (1) Comply with General Order No. 11-10, § 5, and District Court Local Rule 16-15; and (2) Participate in ADR Process* (the "Opposition"),[4] and hereby state as follows:

1. I have personal knowledge of the facts stated in this Declaration, except as to those stated on information and belief, and, as to those, I am informed and believe them to be true. If called as a witness, I could and would competently testify to the matters stated herein.

2. I am a Partner at Dentons US LLP, at 601 South Figueroa Street, Suite 2500, Los Angeles, California 90017-5704, and am one of the attorneys primarily responsible for representing Verity Health System of California, Inc., a California nonprofit benefit corporation and the Debtor herein, and the above-referenced affiliated debtors, the debtors and debtors in possession in the above-captioned chapter 11 bankruptcy cases (collectively, the "Debtors").

3. On January 3, 2020, the Debtors filed the Complaint against SGM and its affiliates, which commenced Adversary Pro. No. 2:20-ap-01001-ER. On January 13, 2020, the Debtors served the Complaint on the defendants, including SGM.

4. As of the date of the Opposition, the Debtors are in the process of closing SVMC on an expedited basis in the interest of patient safety.

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[4] Capitalized terms not otherwise defined herein have the definitions set forth in the Opposition.

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

Executed this 15th day of January, 2020, in Los Angeles, California.

/s/ Tania M. Moyron
Tania M. Moyron

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CERTIFICATE OF COMPLIANCE

1. This Opposition complies with the word limit of FED. R. BANKR. P. 8013(f) because, excluding the parts of the Opposition exempted by FED. R. BANKR. P.8013(a)(2)(C) and FED. R. BANKR. P. 8015(g), this Opposition contains 2,351 words.

2. This Opposition complies with the typeface requirements of FED. R. BANKR. P. 8015(a)(5) and the type-style requirements of FED. R. BANKR. P. 8015(a)(6) because this document has been prepared in a proportionally spaced typeface using Microsoft Word in 14-point Times New Roman.

Dated: January 15, 2020

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CERTIFICATE OF SERVICE

I hereby certify that on January 15, 2020, I electronically filed the foregoing document with the Clerk of the Court for the United States District Court for the Central District of California by using the CM/ECF system.

I further certify that parties of record to this appeal who either are registered CM/ECF users, or who have registered for electronic notice, or who have consented in writing to electronic service, will be served through the CM/ECF system.

I further certify that some of the parties of record to this appeal have not consented to electronic service. I have served the foregoing document by the means set forth below:

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