

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

2:18-20151 Verity Health System of California, Inc.

Chapter 11

Adv#: 2:20-01001 VERITY HEALTH SYSTEM OF CALIFORNIA, INC., a Califo v.

#17.00 Hearing set re [15] *Strategic Global Management, Inc.’s Emergency Motion to Stay Adversary Proceeding*

Docket 0

Matter Notes:

2/11/2020

The tentative ruling will be the order.
Party to lodge order: As set forth in the Amended Tentative Ruling

POST PDF OF TENTATIVE OR AMENDED TENTATIVE RULING TO CIAO

Tentative Ruling:

2/11/2020

(Amended after hearing in RED.) For the reasons set forth below, SGM’s motion to stay this adversary proceeding (the "Stay Motion") is DENIED. Subject to any additional argument that may be presented at the hearing, the Committee’s emergency motion to intervene, for the limited purpose of opposing the Stay Motion, is GRANTED.

Pleadings Filed and Reviewed:

- 1) Strategic Global Management, Inc.’s Emergency Motion to Stay Adversary Proceeding (the "Stay Motion") [Adv. Doc. No. 19]
- 2) Debtors’ Opposition to Strategic Global Management, Inc.’s Emergency Motion to Stay Adversary Proceeding [Adv. Doc. No. 24]
- 3) Official Committee of Unsecured Creditors’ Opposition to Strategic Global Management, Inc.’s Emergency Motion to Stay Adversary Proceeding [Adv. Doc. No. 25]



**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc. Chapter 11

- 4) Reply to Oppositions to "Strategic Global Management, Inc.'s ... Motion to Stay Adversary Proceeding" [Adv. Doc. No. 26]
- 5) Official Committee of Unsecured Creditors' Emergency Notice of Motion and Motion to Intervene Re: Strategic Global Management, Inc.'s Emergency Motion to Stay Adversary Proceeding (the "Intervention Motion") [Adv. Doc. No. 27]

I. Facts and Summary of Pleadings

On August 31, 2018 (the "Petition Date"), Verity Health System of California ("VHS") and certain of its subsidiaries (collectively, the "Debtors") filed voluntary petitions for relief under Chapter 11 of the Bankruptcy Code. The Debtors' cases are being jointly administered. *See* Doc. No. 17.

As of the Petition Date, the Debtors operated six acute care hospitals in the state of California. On December 27, 2018, the Court authorized the Debtors to sell two of their hospitals—O'Connor Hospital and Saint Louise Regional Hospital—to Santa Clara County (the "Santa Clara Sale"). The Santa Clara Sale closed on February 28, 2019.

A. The Asset Purchase Agreement Between the Debtors and Strategic Global Management

On February 6, 2019, the Court conducted a hearing to establish bidding procedures for the auction of the Debtors' four remaining hospitals—St. Francis Medical Center ("St. Francis"), St. Vincent Medical Center (including St. Vincent Dialysis Center) ("St. Vincent"), Seton Medical Center ("Seton"), and Seton Medical Center Coastsides ("Seton Coastsides") (collectively, the "Hospitals"). That hearing required the Court to determine whether to approve an Asset Purchase Agreement (the "APA") between the Debtors and Strategic Global Management ("SGM"). The APA provided that SGM would serve as the stalking-horse bidder for the auction of the Hospitals.

At the February 6, 2019 hearing, the Court found that the termination rights granted to SGM in the APA were unduly broad. In response to the Court's concerns, the Debtors renegotiated the APA to limit SGM's termination rights. On February 19, 2019, the Court entered an order establishing bidding procedures for the auction of the Hospitals and approving the renegotiated APA (the "Bidding Procedures Order") [Bankr. Doc. No. 1572].

The renegotiated provision of the APA—set forth in Section 8.6—pertained to SGM's ability to terminate the transaction in the event that the California Attorney

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

General (the "Attorney General") sought to impose conditions on the sale that were not substantially consistent with those conditions that SGM had agreed to accept (the "Purchaser Approved Conditions"). In the event that the Attorney General sought to impose conditions materially different from the Purchaser Approved Conditions (the "Additional Conditions"), the APA provided the Debtors an opportunity to seek an order from the Court that the Hospitals could be sold free and clear of the Additional Conditions under § 363(f) of the Bankruptcy Code (an order granting such relief, the "Supplemental Sale Order").

Notwithstanding thorough marketing efforts, the Debtors did not receive any qualified bids for all of the Hospitals. The Debtors received one bid to purchase only St. Vincent and one bid to purchase only St. Francis. After consulting with the Official Committee of Unsecured Creditors (the "Committee") and the largest secured creditors, the Debtors determined not to conduct an auction. On May 2, 2019, the Court entered an order finding that SGM was the winning bidder and approving the sale of the Hospitals to SGM for \$610 million (the "SGM Sale"). *See* Bankr. Doc. No. 2306 (the "Sale Order").

B. The Supplemental Sale Order

Pursuant to Cal. Corp. Code § 5914, the Debtors submitted the SGM Sale to the Attorney General for review. On September 25, 2019, the Attorney General consented to the SGM Sale, subject to Additional Conditions that were materially different from the Purchaser Approved Conditions. In response, the Debtors moved for entry of a Supplemental Sale Order. On October 23, 2019, the Court issued a *Memorandum of Decision Granting the Debtors' Emergency Motion to Enforce the Sale Order* (the "Sale Enforcement Memorandum") [Bankr. Doc. No. 3446]. The Sale Enforcement Memorandum found that the Debtors were entitled to entry of a Supplemental Sale Order, on the ground that § 363 of the Bankruptcy Code authorized the Debtors to sell the Hospitals free and clear of the Additional Conditions. The Sale Enforcement Memorandum directed the Debtors to lodge a proposed form of the Supplemental Sale Order.

Between October 23 and November 8, 2019, the Debtors, the Attorney General, and SGM attempted to negotiate a consensual form of the Supplemental Sale Order. *See* Bankr. Doc. No. 3573 (Debtors' description of attempts to arrive upon a consensual form of order). The Debtors reached an agreement with the Attorney General, under which the Attorney General would not appeal the Supplemental Sale Order, but only if the Court entered the Supplemental Sale Order in the exact form

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

negotiated by the Debtors and the Attorney General.

SGM objected to the form of order negotiated between the Debtors and the Attorney General. On November 13, 2019, the Court conducted a hearing on SGM's objections. The Court overruled SGM's objections and entered the Supplemental Sale Order in the form negotiated between the Debtors and the Attorney General. *See* Doc. Nos. 3620 (transcript of hearing addressing SGM's objections) and 3611 (form of the Supplemental Sale Order entered by the Court). On November 29, 2019, SGM appealed the Supplemental Sale Order. *See* Bankr. Doc. No. 3726 (Notice of Appeal). The appeal is currently pending before the District Court (Case No. 2:19-cv-10352-DSF).

C. The Section 8.6 Memorandum of Decision and Order

At the hearing on SGM's objections to the form of the Supplemental Sale Order, SGM argued that after entry of the Supplemental Sale Order, it would have 21 business days to evaluate, in the exercise of its reasonable business judgment, whether the Supplemental Sale Order was acceptable (the "Evaluation Period"), pursuant to § 8.6 of the APA.

On November 18, 2019, the Court entered a memorandum of decision and accompanying order rejecting SGM's argument that it was entitled to the Evaluation Period. *See* Bankr. Doc. Nos. 3632 (the "Section 8.6 Memorandum") and 3633 (the "Section 8.6 Order"). The Court found that under the plain language of the APA, SGM was entitled to the Evaluation Period only if the Supplemental Sale Order was subject to a pending appeal. *See* Section 8.6 Memorandum at 3. The Court further found that based upon representations SGM had made at a February 6, 2019 hearing regarding the purpose of § 8.6 of the APA, SGM was judicially estopped from asserting that it was entitled to the Evaluation Period. *Id.* at 3–4. The Section 8.6 Order provided in relevant part: "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." Section 8.6 Order at ¶ 1.

On November 29, 2019, SGM appealed the Section 8.6 Order. *See* Bankr. Doc. No. 3727 (Notice of Appeal). The appeal is currently pending before the District Court, and has been consolidated with SGM's appeal of the Supplemental Sale Order.

D. The Material Adverse Effect Memorandum of Decision and Order

On November 27, 2019, the Court entered a memorandum of decision and

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

accompanying order rejecting SGM's allegation that the Debtors had failed to comply with certain of the conditions and obligations imposed upon them by the APA, and that these alleged failures to perform had resulted in a Material Adverse Effect which relieved SGM of its obligation to close the SGM Sale. *See* Bankr. Doc. Nos. 3723 (the "Material Adverse Effect Memorandum") and 3724 (the "Material Adverse Effect Order"). The Court stated: "Article 1.3 [of the APA] obligates SGM to close the sale 'promptly but no later than ten (10) business days following the satisfaction' of all conditions precedent. As all conditions precedent were satisfied on November 19, 2019, SGM is obligated to close the sale by no later than December 5, 2019." Material Adverse Effect Memorandum at 7. The Material Adverse Effect Order provided in relevant part: "Pursuant to § 1.3 of the APA, SGM is obligated to close the SGM Sale by no later than December 5, 2019." Material Adverse Effect Order at ¶ 1.

On December 3, 2019, SGM appealed the Material Adverse Effect Order. *See* Bankr. Doc. No. 3746 (Notice of Appeal). The appeal is currently pending before the District Court, and has been consolidated with SGM's appeals of the Section 8.6 Order and Supplemental Sale Order.

E. The Memorandum of Decision and Order Denying the Debtors' Application for Issuance of an Order Requiring SGM to Show Cause Why it Failed to Close the SGM Sale

SGM did not close the SGM Sale by December 5, 2019. On December 6, 2019, the Debtors moved for issuance of an order requiring SGM to show cause why it had failed to close the sale. *See* Bankr. Doc. No. 3773. On December 9, 2019, the Court issued a memorandum of decision and accompanying order denying the Debtors' application for an Order to Show Cause. *See* Bankr. Doc. Nos. 3783 (the "OSC Memorandum") and 3784 (the "OSC Order"). The Court held:

Requiring SGM's representatives to testify as to SGM's reasons for not closing the SGM Sale would not increase the likelihood of the sale actually closing. By failing to close, SGM risks the loss of its \$30 million good-faith deposit as well as the possibility of damages for breach of contract in an amount of up to \$60 million. Being compelled to offer testimony will not motivate SGM to close where the threat of the loss of up to \$90 million has failed to accomplish that end. In the future, the Debtors will have the opportunity to litigate the issues of whether SGM has breached the APA and whether the Debtors are entitled to retain SGM's good-faith deposit. In the

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT...

Verity Health System of California, Inc.

Chapter 11

meantime, the Debtors' efforts would be better spent ensuring the health and safety of the patients at the affected Hospitals.

OSC Memorandum at 2.

F. The Debtors' Complaint

On January 3, 2020, the Debtors filed a *Complaint for Breach of Contract, Promissory Fraud, and Tortious Breach of Contract (Breach of Implied Covenant of Good Faith and Fair Dealing)* (the "Complaint") [Adv. Doc. No. 1] against SGM, KPC Healthcare Holdings, Inc., KPC Health Plan Holdings, Inc., KPC Healthcare, Inc., KPC Global Management, LLC, and Kali P. Chaudhuri, M.D. (collectively, the "Defendants," and all KPC entities collectively, "KPC"). The material allegations of the Complaint may be summarized as follows:

Debtors entered into the APA with SGM based upon SGM's representations that it would have the ability to pay the \$610 million purchase price and that it would work diligently to close the sale. Complaint at ¶¶ 40–45. SGM never anticipated that the Debtors would obtain a final, non-appealable Supplemental Sale Order. *Id.* at ¶ 58. Instead, SGM believed that even if the Debtors obtained the Supplemental Sale Order, that order would remain subject to an appeal, triggering the Evaluation Period under § 8.6 of the APA and giving SGM the option to withdraw from the transaction and/or coerce the Debtors to agree to a substantially reduced purchase price. *Id.* at ¶ 76. Had the Debtors known that SGM was not serious about paying the \$610 million purchase price, they would have pursued other options for the sale and disposition of the Hospitals. *Id.* at ¶ 45.

Debtors expended tremendous time, expenses, and resources to prepare for and close the SGM Sale in reliance on the APA and Sale Order. *Id.* at ¶ 59. Among other things, Debtors (a) sent "WARN Notices" to approximately 4,900 employees, pursuant to the Worker Adjustment and Retraining Notification Act of 1988, at three different times, as KPC continued to postpone the closing date; (b) spent months facilitating an efficient close of the sale, with approximately twenty different workstreams, meeting at least weekly with employees of KPC to ensure a smooth transition of operations and continued care of patients; (c) successfully negotiated and finalized modified collective bargaining agreements with the six unions representing the Hospitals' employees; and (d) coordinated changes in insurance coverages and insurance policies to ensure seamless coverage for employees and patients. *Id.* at ¶ 60.

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

Despite the Debtors' good faith efforts to work towards a prompt closing of the SGM Sale, Defendants dragged their feet and frustrated Debtors' efforts. Defendants failed to ensure that financing, resources, management, and personnel were in place for Defendants to assume operations of the Hospitals in 2019. Defendants did so knowing that the Debtors were continuing to operate at a loss of approximately \$450,000 a day. *Id.* at ¶ 78. Among other things, Defendants (a) failed to timely engage with the Hospitals' primary revenue providers—health plans and physician groups—to provide assurances that their business relationships with the Hospitals would continue after the closing date; (b) failed to onboard a sufficient management team to run the Hospitals, and engaged in eleventh-hour efforts to hire away key members of the Debtors' management team; and (c) delayed decisions on the assumption or rejection of thousands of executory contracts, which created uncertainty for the counterparties to those contracts. *Id.* at ¶¶ 79–81.

On November 18, 2019, SGM's CEO, Peter Baranoff, telephoned Carsten Beith, at the Debtors' investment banker Cain, and stated that SGM could not obtain sufficient financing to close the SGM Sale. *Id.* at ¶ 86. Recognizing that the existence of financing is not a condition to close, SGM resorted to making unfounded and self-serving assertions that the Debtors breached the APA. *Id.* at ¶ 87. On November 22, 2019, SGM sent the Debtors letters setting forth issues that SGM asserted amounted to a Material Adverse Effect (the "November 22, 2019 Letters"). *Id.* at ¶ 88. The issues that SGM raised were not new—they were all known or discoverable during the diligence period that had expired at least nine months earlier. *Id.* And none of the issues altered SGM's obligation to close the SGM Sale by December 5, 2019, because the APA provided that the sale was "as is, where is." *Id.* Even after the Bankruptcy Court entered the Material Adverse Effect Order, which provided that SGM was required to close the SGM Sale by December 5, 2019, SGM refused to close the sale. *Id.* at ¶ 97.

Based upon the foregoing allegations, the Complaint asserts claims for breach of contract, promissory fraud, and tortious breach of contract for breach of the implied covenant of good faith and fair dealing. In Count I, for breach of contract, Debtors allege that the Defendants have materially and continually breached the APA by (a) failing to consummate and close the SGM Sale in accordance with the APA; (b) failing to have funds available to close the SGM Sale at the price set forth in the APA; (c) representing in § 3.9 of the APA and elsewhere that they had the ability to obtain "funds in cash in amounts equal to the purchase price"; (d) attempting to coerce the

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

Debtors to agree to a substantially reduced purchase price; (e) failing to cooperate with the Debtors and move with alacrity towards closing the SGM Sale; (f) making unfunded and untimely assertions of alleged Material Adverse Effects; (g) asserting entitlement to an "Evaluation Period" when no such period existed after entry of the Sale Enforcement Order, the Section 8.6 Order and the Material Adverse Effect Order; (h) appealing the Sale Enforcement Order to avoid its obligation to close and despite the APA's requirement that the Defendants cooperate to render it a final, nonappealable order; and (i) filing meritless and frivolous Notices of Appeal. *Id.* at ¶ 100.

In Count II, for promissory fraud, Debtors allege that at the time Defendants entered into the APA, Defendants had no intention of performing in accordance with the APA, and that Defendants concealed their true intention not to fund the \$610 million purchase price for the purpose of holding the estate, creditors, and patients at the Hospitals hostage in an attempt to extort a lower purchase price. *Id.* at ¶ 102.

In Count III, for tortious breach of contract, Debtors allege that Defendants tortiously breached the APA and the implied covenant of good faith and fair dealing by (a) entering into the APA with no intention to perform their obligations thereunder; (b) failing to consummate and close the SGM Sale in accordance with the APA; (c) failing to have funds available to close the SGM Sale at the \$610 million purchase price set forth in the APA; (d) attempting to coerce Plaintiffs to engage in a re-trade at a lower price; (e) failing to cooperate with Debtors and move with alacrity towards closing the SGM Sale; (f) making unfounded and untimely assertions of alleged Material Adverse Effects; (g) asserting entitlement to an Evaluation Period to which Defendants were not entitled; (h) filing meritless Notices of Appeal; and (i) failing to respond to Debtors' inquiries regarding SGM's intent and financial ability to perform under the APA. *Id.* at ¶ 107.

G. SGM's Emergency Motion to Stay the Adversary Proceeding

On January 16, 2020, SGM filed an emergency motion to stay the adversary proceeding that had been commenced by the filing of the Complaint (the "Stay Motion"). The Court declined to set a hearing on the Stay Motion on 48 hours' notice, as requested by SGM. Instead, the Court *sua sponte* extended the deadline for Defendants to respond to the Complaint to February 19, 2020, to enable the Stay Motion to be heard on regular notice. *See* Doc. No. 15.

In the Stay Motion, SGM asserts that the Court lacks jurisdiction to adjudicate the adversary proceeding until final resolution of SGM's appeals of the Sale Enforcement

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

Order, the Section 8.6 Order, and the Material Adverse Effect Order (collectively, the "Orders"). SGM argues that the issues raised by the Orders touch directly on the issues raised in the adversary proceeding. SGM contends that the Complaint relies heavily on the finding in the Material Adverse Effect Order that the Debtors had complied with all the conditions required for closing and that SGM was obligated to close on December 5, 2019. SGM further maintains that the Complaint overlaps with the Orders because the Complaint alleges that SGM breached the APA by (a) asserting entitlement to an Evaluation Period when no such period existed after entry of the Orders; (b) appealing the Sale Enforcement Order to avoid its obligation to close and despite the APA's requirement that Defendants cooperate to render the Sale Enforcement Order final and non-appealable; and (c) filing meritless and frivolous Notices of Appeal of the Orders.

H. The Debtors' Opposition to the Stay Motion

The Debtors arguments in opposition to the Stay Motion may be summarized as follows:

The divestiture rule provides that the filing of a notice of appeal "confers jurisdiction on the court of appeals and divests the district court of those aspects of the case involved in the appeal." *Griggs v. Provident Consumer Discount Co.*, 459 U.S. 56, 58 (1982). The Ninth Circuit has held:

The "divestiture of jurisdiction rule is not based upon statutory provisions or the rules of civil or criminal procedure. Instead, it is a judge made rule originally devised in the context of civil appeals to avoid confusion or waste of time resulting from having the same issues before two courts at the same time." *United States v. Claiborne*, 727 F.2d 842, 850 (9th Cir. 1984). Though *Griggs* referred to the "divestiture rule" as jurisdictional, the Supreme Court has since made clear that "[o]nly Congress may determine a lower federal court's subject-matter jurisdiction." *Hamer v. Neighborhood Hous. Services of Chicago*, — U.S. —, 138 S.Ct. 13, 17, 199 L.Ed.2d 249 (2017) (quoting *Kontrick v. Ryan*, 540 U.S. 443, 452, 124 S.Ct. 906, 157 L.Ed.2d 867 (2004)). Accordingly, "jurisdictional" rules derived from sources other than Congress are more accurately characterized as "mandatory claim-processing rules" that may be applied in a "less stern" manner than true jurisdictional rules.

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

Rodriguez v. Cty. of Los Angeles, 891 F.3d 776, 790–91 (9th Cir. 2018).

As a pragmatic rule, divestiture (a) does not preclude the Court from exercising jurisdiction over all other matters that it must undertake to implement or enforce the judgment or order, and (b) in the absence of a stay pending appeal, only prohibits modification of the order on appeal. A careful reading of the Orders and the Complaint shows that application of the divestiture rule is not appropriate here. The Orders cover discrete issues concerning the Debtors' efforts to close the now-terminated SGM Sale. The Orders are not dispositive of the claims asserted in the Complaint. The Court acknowledged as much in the OSC Memorandum, which stated that "[i]n the future, the Debtors will have an opportunity to litigate the issues of whether SGM has breached the APA and whether the Debtors are entitled to retain SGM's good-faith deposit." OSC Memorandum at 2. The divestiture rule only prohibits the Court from altering or amending the Orders, and the Complaint does not seek such relief. *See Sherman v. SEC (In re Sherman)*, 491 F.3d 948, 967 (9th Cir. 2007) (internal citation omitted) (holding that where divestiture applies, the "bankruptcy court retains jurisdiction over all other matters that it must undertake 'to implement or enforce the judgment or order,' although it 'may not alter or expand upon the judgment.' If a party wants to stay all of the proceedings in bankruptcy court while an appeal is pending, it must file a motion for a stay.").

The divestiture rule is not properly invoked with respect to the Section 8.6 Order and Material Adverse Effect Order, because both orders are interlocutory. "Filing an appeal from an unappealable decision does not divest the district court of jurisdiction." *United States v. Hickey*, 580 F.3d 922, 928 (9th Cir. 2009). The Section 8.6 Order is interlocutory because its findings were limited to the Debtors' satisfaction of § 8.6 of the APA, and it did not address whether other conditions to closing had been satisfied. *See* Section 8.6 Order at 2 (finding that "SGM is now obligated to promptly close the SGM Sale, *provided that* all other conditions to closing are satisfied") (emphasis added). The Material Adverse Effect Order is interlocutory because it did not compel SGM to close the SGM Sale. Rather, it interpreted the Material Adverse Effect clause and closing conditions in the APA, determined that those provisions were satisfied, and, in light of those findings and the Debtors' outstanding contractual demand, determined that December 5, 2019 was the closing date under § 1.3 of the APA.

Even if the divestiture rule did apply—which it does not—the Court could still adjudicate the Complaint because the divestiture rule is subject to exceptions. As explained by the United States District Court for the Northern District of California:

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

[T]here are generally three situations where a notice of appeal does not divest the district court of jurisdiction: (1) where the issue before the district court is separate from, or collateral to, the matter involved in the appeal; (2) where application of the divestiture of jurisdiction rule would wholly undermine its purpose; and (3) where the appeal is clearly defective or frivolous, usually by reason of untimeliness, lack of essential recitals, or reference to a nonappealable order.

Ashker v. Cate, No. 09-cv-05796-CW, 2019 WL 1558932, at *3 (N.D. Cal. Apr. 10, 2019)
(quotations omitted).

The appeals of the Orders are constitutionally and equitably moot. As a result, the appeals are clearly defective and frivolous, and application of the divestiture rule would wholly undermine its purpose.

The relief set forth in each of the Orders contemplates the effectiveness and closing of the SGM Sale pursuant to the APA. The Court cannot grant relief with respect to closing the SGM Sale given the dramatic change in circumstances after SGM's refusal to close. The APA was terminated on December 27, 2019. The Debtors obtained orders authorizing them to undertake alternative transactions and authorizing the closure of St. Vincent Medical Center. It is no longer possible for the Debtors to close the transaction contemplated by the APA. Consequently, the Orders—which each pertain to the closing of the SGM Sale—are moot.

Finally, SGM has waived its ability to assert that the divestiture rule applies. The APA provides that disputes regarding the occurrence of a Material Adverse Effect "shall be exclusively settled by a determination made by the Bankruptcy Court" APA at § 9.1(c). This provision constitutes an enforceable contractual appeal waiver. *See Minesen Co. v. McHugh*, 671 F. 3d 1332, 1339 (D.C. Cir. 2012) (extensive case law permits voluntary waivers of rights to appeal); *Slattery v. Ancient Order of Hibernians in Am.*, No. 97-7173, 1998 WL 135601, at *1 (D.C. Cir. Feb. 9, 1998) (dismissing appeal where parties "agree[d] not to appeal any decision by the district court relating to defendants' motion for attorneys' fees"). Because SGM has waived its appellate rights with respect to Material Adverse Effect determination, it cannot invoke the divestiture rule.

Section 12.3 of the APA provides that "the parties irrevocably elect, as the sole judicial forum for the adjudication of any matters arising under or in connection with

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

the Agreement, and consent to the exclusive jurisdiction of, the Bankruptcy Court." As a result of this waiver, SGM cannot invoke the divestiture rule with respect to the Sale Enforcement Order or the Section 8.6 Order.

I. The Committee's Opposition to the Stay Motion and the Committee's Motion to Intervene

The Official Committee of Unsecured Creditors (the "Committee") filed an opposition to the Stay Motion (the "Committee Opposition"). In its reply briefing, SGM asserted that the Committee Opposition should be stricken because the Committee (1) is not a party to the adversary proceeding, (2) has not obtained Court permission to intervene in the adversary proceeding, and (3) has no standing to participate in the adversary proceeding.

The Court authorized the Committee to notice a hearing on an emergency motion to intervene (the "Intervention Motion") concurrently with the hearing on the Stay Motion. The Committee seeks to intervene for the limited purpose of opposing the Stay Motion. The Committee has not yet decided whether it will move to intervene as to the remainder of the adversary proceeding.

In support of the Intervention Motion, the Committee argues that multiple circuit courts have held that, under § 1109(b), a creditors' committee may appear and be heard in *any proceeding* in the bankruptcy court—including adversary proceedings. *See, e.g., In re Caldor Corp.*, 303 F.3d 161, 175-76 (2nd Cir. 2002) (term loan holder committee had unconditional right under Section 1109(b) to intervene in adversary proceeding against Chapter 11 debtors); *Matter of Marin Motor Oil, Inc.*, 689 F.2d 445, 451-54 (3rd Cir. 1982) (under Section 1109(b), creditors' committee had "absolute right" to intervene in adversary proceeding). In the alternative, the Committee asserts that it meets the requirements for intervention as of right under Civil Rule 24(a)(2). Specifically, the Committee maintains that it has a significant protectable interest in this matter, given that the Debtors' claims against SGM for breach of contract represent a significant source of money that might be available to provide a recovery to unsecured creditors.

The Committee's arguments in opposition to the Stay Motion may be summarized as follows:

The Stay Motion is nothing more than an attempt by SGM to indefinitely delay resolution of the Complaint. SGM's breach of the APA cost the estates not less than \$100 million, resulted in a material loss of jobs, and adversely impacted local access

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

to healthcare.

The Committee is concerned that, in the course of the delay that SGM seeks, SGM's principals will strip SGM of its assets, negating its ability to satisfy a future judgment.

SGM's misconduct is illustrated by its appeal of the Supplemental Sale Order. The rationale for § 8.6 of the APA was that it might prove risky for SGM to close the sale if the Supplemental Sale Order was appealed, given that an appeal could expose SGM to the more onerous Additional Conditions that it had not agreed to accept. To that end, § 8.6 gave SGM the option to walk away if an appeal of the Supplemental Sale Order remained pending at the time of closing. It was never contemplated that SGM itself could trigger such optionality (i.e., grant itself a right to walk away) by filing an appeal of the very Supplemental Sale Order it needed for comfort. But this now appears to be precisely SGM's position.

J. SGM's Reply in Support of the Stay Motion

SGM's arguments in reply to the Debtors' opposition may be summarized as follows:

The divestiture rule applies where, as here, the issues in the lower court "involve aspects of the case that are the subject of the pending appeal." *Mercado-Guillen v. McAleenan*, 2019 WL 1995331, at *2 (N.D. Cal. May 6, 2019). At base, the Complaint seeks to hold SGM liable for failing to close the SGM Sale in accordance with the APA. Complaint at ¶ 100. However, it is undisputed that SGM had no duty to close the SGM Sale until the Debtors had satisfied all conditions precedent to closing. SGM has appealed the Material Adverse Effect Order, which found that the Debtors had satisfied all conditions precedent. The Bankruptcy Court cannot adjudicate the issue of whether the Debtors had satisfied the conditions precedent to closing while that same issue is being considered by the District Court in connection with the appeal.

The Debtors assert that the Court need not stay the adversary proceeding because SGM did not seek a stay of any of the appealed Orders. However, the Orders from which SGM appealed are not enforceable orders; if they were, the Debtors would not have filed the Complaint to obtain damages. SGM had no need to seek a stay until the Debtors filed the Complaint, which created the prospect of two courts ruling on the same issues at the same time.

The Debtors assert that the divestiture rule does not apply because SGM's appeals

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

are frivolous. It is not appropriate for the Bankruptcy Court to determine whether the appeals are frivolous; such a determination would usurp the authority of the District Court.

Along similar lines, the Debtors assert that the divestiture rule does not apply because the Orders were interlocutory. Questions about the District Court's jurisdiction over the appeals should be left to the District Court. However, the Debtors' contention that the Orders were interlocutory is mistaken. The Material Adverse Effect Memorandum unambiguously and finally decided that "all conditions precedent to closing have been satisfied" and that "SGM is obligated to close the sale by no later than December 5, 2019." Material Adverse Effect Memorandum at 7. This was a final order—after its entry, there were no other sale conditions left for the Court to interpret, and SGM was obligated to close the sale.

If SGM is not permitted to proceed with its appeals of the Orders prior to adjudication of the Complaint, then SGM will be subject to the Debtors' argument that the Orders preclude SGM from contesting the Complaint's allegations—in particular, the allegation that SGM failed to timely close the sale notwithstanding its obligation to do so. This would enable the Debtors to obtain a judgment in their favor on their breach of contract claims without the Defendants ever having had the opportunity to present evidence in defense of those claims.

There is no merit to the Debtors' contention that the appeals are moot because the APA has been terminated. It is true that it is no longer possible for the sale contemplated by the APA to close. But that has nothing to do with the Complaint, which requires a determination over which party breached the APA.

The Debtors' argument that SGM waived its rights to appeal or to invoke the divestiture rule are likewise without merit. The waiver of a right to appeal must be express. *In re Deepwater Horizon*, 785 F.3d 986, 997 (5th Cir. 2015). The "exclusively settled" and "sole judicial forum" language in §§ 9.3(c) and 12.3 of the APA simply provides the forum in which disputes arising under the APA would be adjudicated. Nothing in either section can reasonably be interpreted as an express waiver of the right to appellate review.

II. Findings and Conclusions

A. The Committee is Authorized to Intervene for the Limited Purpose of Opposing the Stay Motion

The Committee is authorized to intervene for the limited purpose of opposing the Stay Motion. The Court declines SGM's request to strike the Committee Opposition.

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

The Second and Third Circuits have both held that, pursuant to § 1109(b), a creditors' committee has an unconditional right to intervene in an adversary proceeding within a Chapter 11 case. *See Term Loan Holder Committee v. Ozer Group, LLC (In re Caldor Corp.)*, 303 F.3d 161, 176 (2d Cir. 2002) and *Committee v. Michaels (Matter of Marin Motor Oil, Inc.)*, 689 F.2d 445, 451 (3d Cir. 1982).

Here, the Committee has sought authorization to intervene solely for the purposes of opposing the Stay Motion. SGM acknowledges that the Committee has the authority to be heard on issues arising in the main bankruptcy case, but contends that the Committee's right to be heard does not apply to the instant adversary proceeding. However, SGM initially filed the Stay Motion in the main bankruptcy case; it re-filed the Stay Motion in the adversary proceeding only after being ordered to do so by the Court. SGM's decision to initially file the Stay Motion in the main bankruptcy case severely undercuts its assertion that the Committee lacks standing with respect to the Stay Motion.

Even if the Stay Motion had not initially been filed in the main bankruptcy case, the Court would find it appropriate to permit the Committee to intervene for the limited purpose of opposing the Stay Motion. The timing of the adjudication of the Complaint will significantly affect the creditors that the Committee represents. In the event the Debtors prevail, the creditors that the Committee represents may be entitled to a portion of the recovery. The Committee has an interest in assuring that the Complaint is not stayed pending the outcome of SGM's appeals of the Orders. That interest is significant enough to confer standing upon the Committee to oppose the Stay Motion.

In the event the Committee wishes to be heard in connection with future issues arising in this adversary proceeding, the Committee shall file a further motion to intervene.

B. The Stay Motion is Denied

"The filing of a notice of appeal is an event of jurisdictional significance—it confers jurisdiction on the court of appeals and divests the district court of its control over those aspects of the case involved in the appeal." *Griggs v. Provident Consumer Disc. Co.*, 459 U.S. 56, 58, 103 S.Ct. 400, 74 L.Ed.2d 225 (1982).

The premise of the Stay Motion is that the Orders contain findings which (a) preclude SGM from defending itself against the Complaint's allegations and (b) require the Court to enter judgment in the Debtors' favor on the breach of contract claim. Based upon this premise, SGM asserts that the adversary proceeding must be

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

stayed until the completion of its appeals of the Orders.

SGM's premise is not correct. The Orders do not adjudicate whether SGM had breached the APA; nor do the Orders contain findings that compel the Court to rule in the Debtors' favor with respect to the Complaint's breach of contract claim. The Orders were entered "[t]o facilitate an expeditious and successful resolution of these cases," Section 8.6 Order at 2. To that end, the Orders contained various findings necessary to allow the SGM Sale to proceed. The sole purpose of those findings was to provide the framework necessary for the Debtors and SGM to promptly close the SGM Sale. The findings were not intended to create a springboard for a claim for breach of contract against SGM.

Significantly, nothing in the Orders determined SGM's liability, if any, for breach of the APA. The limited scope of the Orders was made clear in the OSC Memorandum, in which the Court emphasized that the issue of whether SGM had breached the APA had not yet been decided: "*In the future*, the Debtors will have the opportunity to litigate the issues of whether SGM has breached the APA and whether the Debtors are entitled to retain SGM's good-faith deposit." OSC Memorandum at 2.

The APA was terminated on December 27, 2019. St. Vincent, one of the Hospitals whose sale was contemplated by the APA, has now closed. The SGM Sale is dead and cannot be resuscitated. The findings in the Orders—which the Court made only to facilitate the closing of the SGM Sale—cannot spring back to life in the entirely different context of the Debtors' breach of contract claim. The Orders do not preclude SGM from contesting the Debtors' allegation that SGM breached the APA. SGM remains free to present evidence in this proceeding in support of its position that as of December 5, 2019, it was not obligated to close the SGM Sale. The corollary is that the Debtors cannot rely solely upon the Material Adverse Effect Order to support their allegation that SGM was obligated to close as of December 5, 2019.

Because the findings in the Orders were limited to the failed SGM Sale, those findings are not dispositive of the claims asserted in the Complaint. Consequently, SGM's appeal of the Orders has not divested this Court of jurisdiction over the separate issues arising in the Complaint.

~~An additional reason for the inapplicability of the divestiture rule is that SGM has waived its right to appeal the Orders. To prevent abusive appeals undertaken "to run up an adversary's costs or to delay trial," the Court may decline to apply the divestiture rule if it certifies that an appeal has been waived. *Rodriguez v. Cty. of Los Angeles*, 891 F.3d 776, 791 (9th Cir. 2018). SGM has waived its right to appeal any of the Orders. With respect to the Material Adverse Effect Order, the APA provides that~~

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

~~"any dispute between Purchaser [SGM] and Sellers [the Debtors] as to whether a Material Adverse Effect has occurred for any purpose under this Agreement shall be exclusively settled by a determination made by the Bankruptcy Court." APA at § 9.1(c) (emphasis added). With respect to the Sale Enforcement Order and the Section 8.6 Order, § 12.3 of the APA provides that "the parties irrevocably elect, as the sole judicial forum for the adjudication of any matters arising under or in connection with the Agreement, and consent to the exclusive jurisdiction of, the Bankruptcy Court" The Court will certify to the District Court that SGM has waived its right to appeal the Orders. For this additional reason, the divestiture rule does not apply.~~

Based upon the foregoing, the Stay Motion is DENIED. The Court will prepare and enter an order denying the Stay Motion and an order granting the Intervention Motion. ~~and a certification that SGM has waived its right to appeal the Orders.~~

No appearance is required if submitting on the court's tentative ruling. If you intend to submit on the tentative ruling, please contact Carlos Nevarez or Daniel Koontz, the Judge's Law Clerks, at 213-894-1522. **If you intend to contest the tentative ruling and appear, please first contact opposing counsel to inform them of your intention to do so.** Should an opposing party file a late opposition or appear at the hearing, the court will determine whether further hearing is required. If you wish to make a telephonic appearance, contact Court Call at 888-882-6878, no later than one hour before the hearing.

Party Information

Debtor(s):

Verity Health System of California,

Represented By

Samuel R Maizel

John A Moe II

Tania M Moyron

Claude D Montgomery

Sam J Alberts

Shirley Cho

Patrick Maxcy

Steven J Kahn

Nicholas A Koffroth

**United States Bankruptcy Court
Central District of California
Los Angeles
Judge Ernest Robles, Presiding
Courtroom 1568 Calendar**

Tuesday, February 11, 2020

Hearing Room 1568

10:00 AM

CONT... Verity Health System of California, Inc.

Chapter 11

Defendant(s):

Kali P. Chaudhuri, M.D., an	Pro Se
Strategic Global Management, Inc.,	Pro Se
KPC Healthcare Holdings, Inc., a	Pro Se
KPC Health Plan Holdings, Inc., a	Pro Se
KPC Healthcare, Inc., a Nevada	Pro Se
KPC Global Management, LLC, a	Pro Se
Does 1 through 500	Pro Se

Plaintiff(s):

ST. VINCENT MEDICAL	Represented By Samuel R Maizel Tania M Moyron
St Vincent Dialysis Center, Inc., a	Represented By Samuel R Maizel Tania M Moyron
ST. FRANCIS MEDICAL	Represented By Samuel R Maizel Tania M Moyron
Seton Medical Center, a California	Represented By Samuel R Maizel Tania M Moyron
Verity Holdings, LLC, a California	Represented By Samuel R Maizel Tania M Moyron
VERITY HEALTH SYSTEM OF	Represented By Samuel R Maizel Tania M Moyron