14-1550

In the United States Bankruptcy Appellate Panel for the Ninth Circuit

IN RE CITY OF STOCKTON, CALIFORNIA,

Debtor.

FRANKLIN HIGH YIELD TAX-FREE INCOME FUND AND FRANKLIN CALIFORNIA HIGH YIELD MUNICIPAL FUND,

Appellants,

v.

CITY OF STOCKTON, CALIFORNIA,

Appellee.

APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE EASTERN DISTRICT OF CALIFORNIA, CASE NO. 12-32118, HON. CHRISTOPHER M. KLEIN

ANSWERING BRIEF OF DEBTOR AND APPELLEE CITY OF STOCKTON, CALIFORNIA

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CORPORATE DISCLOSURE STATEMENT

Appellee City of Stockton is not a corporate party under Federal Rule of Appellate Procedure 26.1.

May 28, 2015

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TABLE OF ABBREVIATIONS**

CalPERS	California Public Employees' Retirement System
CBA	Collective Bargaining Agreement
FY	Fiscal Year
GFOA	Government Finance Officers Association
LRFP	Long-Range Financial Plan
NPFG	National Public Finance Guarantee Corporation
PFFs	Public Facilities Fees
POBs	Pension Obligation Bonds
SPOA	Stockton Police Officers' Association

** We cite Franklin's Opening Brief as "OB;" Franklin's Excerpts of Record as "ER"; and our Supplemental Excerpts of Record as "SER." We refer to Bankruptcy Judge Christopher M. Klein of the United States Bankruptcy Court for the Eastern District of California, who presided over this chapter 9 case, as "the Bankruptcy Court" or "the Court."

INTRODUCTION

The City of Stockton has emerged from bankruptcy with a renewed hope of financial stability and positioned to avoid a future chapter 9 filing, but getting to this point was not easy. By the time it sought chapter 9 relief as a last resort, the City was already deep into a downward spiral. A drastic budget shortfall required dramatic staffing cuts, depleting the police and fire departments in particular, a default on debt, the cessation of numerous community services, and a worsening state of decay of facilities for lack of repair or replacement. This was the cloud under which the City entered mediations with its unions and major creditors and then later sought chapter 9 relief.

As the months wore on, the City and its various creditors, aided by the mediation services of Bankruptcy Judge Elizabeth Perris, inched closer to terms all could accept. Ultimately, more than six years after the City first declared a fiscal emergency, and more than two-and-a-half years after it entered chapter 9, Chief Bankruptcy Judge Christopher Klein confirmed a plan of adjustment ("the Plan") that enjoyed the support of all but one material creditor. Despite extensive negotiations, the City and appellants Franklin High Yield Tax-Free Income Fund and Franklin California High

Yield Municipal Fund (collectively, "Franklin") could not reach a deal. Franklin litigated its claim and contested confirmation instead.

Having received cash payment of more than $6 million, approximately 17.5% of its claim, but nevertheless unhappy about the results of its gamble, Franklin seeks to relitigate here. But its attacks are founded on the same skewed version of the facts Judge Klein rejected following a five-day confirmation hearing and review of the evidence, countless pleadings, and stacks of trial declarations. Franklin also posits the same flawed legal standards that Judge Klein properly rejected and that, if accepted, would make meaningful chapter 9 relief impossible in virtually every case.

Franklin objects to the Plan's classification and treatment of its unsecured deficiency claim, complaining that it should not have to vote alongside other creditors holding unsecured claims, including City retirees who lost $545 million of health benefits. It bemoans the size of its return compared with that of other bond creditors—all of which negotiated settlements—but conspicuously fails to mention the collateral securing the claims of those other creditors. As in chapter 11, collateral counts in chapter 9 cases, where debts are secured by interests in cash flow from taxes or in possessory interests in leases of police stations, fire stations, libraries, parking facilities, and other assets essential to a municipality's economic recovery and very existence. Franklin's collateral—possessory interests in two money-losing golf courses and a park—was plainly not essential to the City. Franklin refuses to face that reality.

So, too, when it comes to the City's decision to assume its pension obligations. Franklin characterizes this decision as evidence that the City did not file the Plan in good faith and an indication that the Plan is not in the best interests of creditors. But Franklin's brief omits even passing mention of the voluminous evidence and testimony explaining the rationale for that decision. The Bankruptcy Court heard about the crippling $1.6 billion termination liability that would inevitably flow from impairing accrued pensions. It heard how the City had considered other pension options, only to conclude that no workable, less-costly alternative existed. And it heard about the devastating impact impairing pensions would have on the City's viability as an employer. Indeed, the Chief of Police related conversations with police officers who promised to leave if the City impaired its pension obligations, a downright scary prospect for a city with an already depleted police force facing one of the highest crime rates in California. Maintaining pensions was not bad faith; it was necessary.

Franklin's repeated claims of punitive treatment are without merit. The City does not begrudge Franklin choosing the bench over the bargaining table; litigating was Franklin's prerogative. The City has always left the light on for Franklin in case it was willing to make a deal that would work for both parties. That did not happen, and Franklin cannot now demand that the City's years of hard work be flushed because Franklin is disappointed with the results of its litigation strategy.

Confirmation of the Plan was proper in every respect, and should be affirmed.

QUESTIONS PRESENTED

1.a. Whether Franklin's unsecured deficiency claim is properly classified with other general unsecured claims and separately from other material claims where Franklin's claim has no other source of repayment that differentiates it from the general unsecured claims and where the City's settlement with, and treatment and classification of, other material creditors is based on sound business, economic, and legal justifications, § 1122.

b. Whether Franklin's unsecured deficiency claim receives equal treatment to the other general unsecured claims in its class where all claims receive the same percentage payment, § 1123(a)(4).

2. Whether the Plan is "in the best interests of creditors and is feasible," § 943(b)(7), where the alternative—dismissal of the chapter 9 case—would result in a chaotic and unproductive race to the courthouse and where the Plan devotes a more than reasonable share of future revenues to repayment of creditors while leaving the City enough to attain a state of lasting solvency.

3. Whether, in light of the City's extensive steps to reduce costs before and during the chapter 9 case and its earnest and largely successful efforts to reach a consensual plan, the City proposed the Plan in good faith, § 1129(a)(3).

4. Whether the Bankruptcy Court properly interpreted the words "amount of … claim" in § 502(b), as distinguished from ten other Bankruptcy Code provisions calling for a determination of "value," not to require that the amount of a claim be discounted to present value.

5. Whether the Bankruptcy Court properly interpreted the words "to be paid" in § 943(b)(3) to require disclosure only of professional fees not yet paid.

STATEMENT OF THE CASE

A. The City of Stockton falls on hard times.

The City of Stockton "was ground zero for the subprime mortgage crisis." SER235 (Eligibility Opinion). After a period of tax revenue growth during the housing bubble, the City entered into a period of economic free fall with one of the nation's highest foreclosure rates. SER13-15, 27.

Unemployment soared to 22.3%. SER15, 18. Residential and commercial property values declined by 50%. SER235 (Eligibility Opinion); SER14, 27. As property values fell and the local economy ground to a near halt, tax revenues plummeted. SER235. Between Fiscal Years ("FY") 2007-08 and 2011-12, property tax collections fell from $59.8 million to $44.4 million, a 26% decrease. SER14. Sales, utility, franchise, and business license taxes dried up, as citizens spent less and business development stalled. SER15.

At the same time, the City faced excessive labor costs and an unsustainable debt load accumulated over years of unrealistically optimistic fiscal management. ER515-16. On the labor side, the City had promised above-market compensation and benefits. ER516; SER2-3, 110. As for the debt load, the City had issued $125 million in pension obligation bonds ("POBs") (which, as a result of pension system investment losses, barely made a dent in unfunded pension liability, SER89-90); $46 million to construct an events center; $32 million for two parking garages and capital projects; $40 million to purchase an office building that was to become the new City Hall; and $35 million for a fire station, police communications center, parks, and street improvements. SER88. These last bonds are owned by Franklin. OB7.

There is no better primer for the fiscal challenges the City faced before bankruptcy than the Bankruptcy Court's opinion ruling the City eligible for chapter 9 relief, *In re City of Stockton, Cal.*, 493 B.R. 772, 778-83 (Bankr. E.D. Cal. 2013) (SER231-79). In short, the City's finances had serious structural problems that the Great Recession laid bare.

B. The City takes drastic measures to cut costs, but cannot avoid insolvency.

The General Fund, the City's only source of unrestricted funds, SER78-79, "accounts for most municipal services [including] police, fire, public works, administrative services, recreation, and cultural programs." SER78-79. By the end of FY2007-08, facing falling revenues, huge labor costs, hundreds of millions of dollars in unfunded employee and retiree benefits, a staggering, backloaded debt structure, and no emergency reserves, the City anxiously watched the General Fund, wondering whether the next periodic deposit of tax revenues would be sufficient to make payroll. SER15-16, 79.

In 2008, in an effort to keep the General Fund solvent, the City began drastically cutting labor costs. It reduced pay and benefits, then furloughed employees, froze hiring, restricted operating hours, and eventually was forced to lay off large numbers of employees. SER3, 15-16. Nevertheless, in May 2010, the City's General Fund budget forecast for upcoming FY2010-11 projected a $23 million deficit. SER17, 79. Lacking the reserves to cover the deficiency, the City Council had no choice but to declare a state of fiscal emergency. SER17, 30-31. The City continued to slash costs over the next two years, SER17-18, 20-23, but the cuts had their own debilitating effects.

Basic necessary services were scaled back. Between FY2008-09 and FY2011-12, the City eliminated 31% of its full time positions in departments supported by the General Fund, including deep cuts to the police and fire departments. SER16-17. A total of 424 positions were eliminated, among them:

- 98 sworn police officers;
- 47 other police department employees;
- 76 fire department employees; and
- 203 other positions, including administration, public works, and library employees.

SER16.

The police and fire departments were stretched way too thin. The number of remaining police officers was simply insufficient to handle the City's sky-high crime rate and gang and narcotics problems. SER238-40, 260 (Eligibility Opinion); SER16, 72-75. The fire department faced equally serious challenges. The City had to close a fire truck company, there were not enough trucks to meet the City's needs, and the department had to dispatch mechanics to the scenes of fires because equipment would often break down en route. SER17, 19.

Citywide decay set in. The City deferred maintenance and cancelled library renovations. SER19-20. It closed a community center and a library branch, and it scaled back after-school programs. SER20. It could not even afford to repair its crumbling City Hall. SER19-20.

In early 2012, the City brought in an outside expert consultant to evaluate the City's solvency. Its report concluded that the City failed to meet the criteria for "service delivery solvency" (the "ability to pay all costs of providing services at [a] level [and] quality required for community health, safety, [and] welfare"); that it failed to meet the criteria for "budget solvency" (the "ability to create a balanced budget with sufficient revenues and reserves to pay for fiscal year[] expenses"); and that "cash solvency" (the "ability to generate [and] maintain cash balance[s] needed to pay bills when they come due") was hanging by a thread. SER126; *see* SER21, 52-53, 63.

The cash crunch was not just on paper. In March 2012, the City failed to pay $2 million in debt service. SER22. It was the first time the City had missed a payment to capital markets creditors. SER22. As a result, a receiver was appointed to run three City-owned parking garages on behalf of the indenture trustee, and the indenture trustee took over a City-owned office building and began to collect rents from private tenants to satisfy the debt. SER242 (Eligibility Opinion).

C. The City mediates with its creditors in the AB 506 process.

The City Council decided that a global outreach to its creditors was the only way to stave off a complete financial meltdown, so in February 2012, it initiated the "AB 506 process," named after a bill that had recently been passed into law (Cal. Gov't Code §§ 53760 *et seq.*). The AB 506 process provides distressed municipalities an opportunity to reach a mediated solution with their creditors and, hopefully, to avoid seeking chapter 9 relief. 2011 Cal. Stat. ch.675, pp. 1-2 (AB 506 legislative history). The City and its creditors jointly selected former Bankruptcy Judge Ralph Mabey as the mediator. SER242.

To facilitate the mediation, the City created what came to be called "the Ask," which the Bankruptcy Court would later describe as "an opening position that formed the basis for conversation with the parties." SER205. It contained a lengthy analysis of the City's current fiscal circumstances and extended fiscal projections, SER110-23, and it proposed adjustment of the City's relationships with major classes of creditors, including labor, retirees, and holders or insurers of the City's bond debts. SER128-61.

The AB 506 process consisted of over 49 mediation sessions in the spring of 2012. SER98-101. Negotiations with labor were highly productive, ultimately yielding significant cost-saving agreements with all but one of the major labor organizations (the Stockton Police Officers' Association ("SPOA")). SER382-83; *infra* 16-17 (detailing the labor agreement adjustments and cost savings). The City could not, however, come to an agreement with any of its major bond creditors. Only one—Franklin—even made a counteroffer, but it "was just too far removed from the relief that the City needed … in order for it to be a viable situation." SER208.

D. The City petitions for chapter 9 relief and establishes its eligibility.

1. The City filed its chapter 9 petition on June 28, 2012. ER2. The case was assigned to Judge Klein. ER2.

On July 10, 2012, Judge Klein appointed Judge Perris to preside over mediations between the City and its major creditors. ER29; SER92-93. Those creditors included:

- SPOA, the only labor union with which the City had yet to reach agreement;
- 2,100 retirees with pension benefits, of which about 1,100 also possessed claims of right to lifetime health benefits ("Retiree Health

Benefit Claims"), ER637, represented in the chapter 9 case by the Official Committee of Retirees ("Retirees Committee");[1]

- California Public Employees' Retirement System ("CalPERS"), a creature of California Public Employees' Retirement Law, Cal. Gov't Code §§ 20460 *et seq*. As the Bankruptcy Court explained, the City's pension obligations in effect generate two relationships. ER309. One is between the City and CalPERS, with which the City contracts to "administer City pensions by collecting payments from the City and investing those funds so as to produce enough to pay the pensions." ER309; SER450. The other, of course, is between the City and the current and future employees to whom it promises pensions. ER309. These individuals, as the Bankruptcy Court recognized, are the creditors who would bear the impact if the City impaired pension obligations. ER328-29;
- Assured Guaranty Corp. and Assured Guaranty Municipal Corp. ("Assured"), which insured and was therefore the real party in

[1] Although the disclosure statement filed with the first amended plan estimated the number of total retirees at 2,400, SER286, a number Franklin's brief references (at 47), the final number of retirees with claims turned out to be approximately 2,100, ER637.

interest with respect to the $125 million POBs, ER254; SER319, as well as $40.8 million in 2007 bond issuances. SER303-04;

- National Public Finance Guarantee Corporation ("NPFG"), which insured $47 million in bonds issued in 2004, SER294; $32.8 million in bonds issued in 2004, SER297; and $14 million in bonds issued in 2006, SER301;
- Franklin, which bought all $35 million of uninsured bonds the City issued in 2009. SER309;
- Ambac Assurance Corporation ("Ambac"), which insured approximately $13.3 million in 2003 certificates of participation. SER290; and
- Wells Fargo Bank, the indenture trustee for the above financing. SER290, 294, 297, 301, 304, 309, 319.

2. Assured, NPFG, and Franklin (along with Wells Fargo), filed oppositions to the City's eligibility for chapter 9 relief under § 109(c). SER208-09. They argued that the City was not insolvent, § 109(c)(3); that the AB 506 process did not constitute good faith negotiation, § 109(c)(5)(B); and that the City's filing of its petition was in bad faith, § 921(c).

In early 2013, the Bankruptcy Court held a three-day trial on eligibility. The Court heard from seven witnesses, received declarations from 15 additional witnesses, and reviewed hundreds of exhibits amounting to thousands of pages.

The Court rejected all of the challenges to the City's eligibility, making extensive, detailed factual findings on the City's insolvency and the daunting challenges it faced to extricate itself. SER235-45, 260-62 (Eligibility Opinion); *see* SER188-209.

The Court also found that there was no basis for the suggestion that the City's position in the AB 506 mediation process was a "take-it-or-leave-it" offer en route to bankruptcy. SER246-54 (Eligibility Opinion). It noted that the mediation sessions yielded "substantial agreements" with the labor organizations and substantial progress in discussions with other stakeholders. SER221, 244 (Eligibility Opinion). As to the lack of progress with the capital markets creditors in the AB 506 process, the Court emphasized the strident positions taken by the objecting creditors and their lack of interest in pursuing discussions with the mediator. SER244-45 (Eligibility Opinion). "[S]erious and productive negotiations with a category of claimants who represent more than two-thirds of a municipality's annual budget independently suffices to satisfy the good faith negotiation requirement." SER250 (Eligibility Opinion).

Emphasizing "the multi-year effort to ratchet down expenses during which the City reduced employees and reduced employee compensation, its cash insolvency, its service insolvency, its good faith negotiations or efforts to negotiate with creditors, and its inability to achieve significant further reductions without being able to compel the impairment of contracts," the Court found the City eligible for chapter 9 relief. SER272 (Eligibility Opinion); *see* SER228-29.

E. The City reaches mediated resolutions.

While Assured, NPFG, and Franklin were contesting eligibility, the mediation sessions with Judge Perris continued and resolved a number of claims.

The City finalized settlements with all nine of its labor unions. The unions made crucial and significant concessions on behalf of the City's employees, affording the City relief from future labor costs by locking in compensation at or below market levels. ER429-30; SER249-50 (Eligibility Opinion). Going forward, these concessions will substantially reduce the City's future pension obligations as well. ER805. The renegotiated collective bargaining agreements ("CBA") also eliminated retiree health care benefits for current employees, providing the City relief from potentially $1 billion in future health care costs. ER805; SER258-59 (Eligibility Opinion). The City obtained further relief from future pension obligations by, among other things, successfully negotiating for larger employee contributions. ER805; SER258-59 (Eligibility Opinion).

The City also reached a mediated resolution with former employees on the Retiree Health Benefit Claims. The City hired the Segal Company ("Segal"), a nationally-recognized actuarial and consulting firm with expertise in public sector benefits, to calculate the Retiree Health Benefit Claims, and the resulting report calculated an aggregate amount of $545 million. ER576. The Plan, pursuant to the settlement, would pay the 1,100 holders of the $545 million of unsecured Retiree Health Benefit Claims an aggregate of $5.1 million in full satisfaction of these claims (i.e., $.01 on the dollar), resulting in huge relief for the General Fund. The other major component of the settlement was the City's agreement not to impair pensions, discussed *infra* 21-24.

Following the eligibility ruling, the City and the capital markets creditors engaged in months of intense negotiations which resulted in term sheet agreements with Ambac, NPFG, and Assured, described below, that dramatically reduced the exposure of the General Fund while preserving vital City assets. *See generally* SER357-62.

Assured. The 2007 lease obligation bonds insured by Assured were secured by a lease of an office building at 400 E. Main Street ("400 E. Main"), the planned replacement for City Hall. SER303-06, 392. The settlement with Assured extinguished the bonds in their entirety, and the City and Assured entered into an option agreement that effectively conveyed 400 E. Main to Assured. SER308-09. As part of the agreement, Assured leased space in that building to the City at below-market rental rates for eight years, with four one-year City renewal options. SER392-94. By negotiating this favorable lease, the City preserved a replacement for its decrepit City Hall and thus a home for many of its essential services. SER361, 392. Also as part of the settlement, the parties agreed that the POBs would be reduced to 52%, but provided for contingent payments allowing for the possibility of full repayment if the City's revenues outperformed certain baseline projections. SER551; *see* SER320-21.

NPFG. The 2004 parking structure bonds were secured by a lease in three revenue-producing downtown parking garages. SER297-99.

Pursuant to the City's settlement with NPFG, the City created a new Parking Authority, transferred ownership in all downtown parking facilities to the Parking Authority, and shifted the payment obligation from the General Fund to the Parking Authority, taking that debt off of the General Fund ledger. SER360. The 2004 arena-related bonds were secured by both a lease in the arena and a pledge of certain restricted tax revenues. SER294-96. The bonds were restructured to provide debt service savings and to make it highly likely that restricted tax revenues will be sufficient to pay the debt. SER324, 552-53. To further insulate the General Fund, the City negotiated a ceiling on the amount for which the General Fund was responsible. SER546-47.

Finally, the parties agreed not to impair NPFG's 2006 bonds, which were secured by a lease in the Stewart Eberhardt Building, which houses the City's departments for Human Resources, 911 Dispatch, Police Investigations and Crime Lab, and Public Works. SER392. The building was constructed to meet California "essential services" building standards, making it particularly expensive to replace. SER302-03.

The NPFG settlement thus provided huge relief for the General Fund while preserving City use of assets vital to its recovery. The City understood that rejuvenating its downtown business sector is "a critical component of [its] future economic viability and recovery." SER392. The arena, which attracts business and creates jobs, and the parking facilities that allow visitors to flock downtown are indispensable to that goal. Meanwhile, the Stewart Eberhardt Building already housed several essential City services.

Ambac. Ambac's claims were secured by leases of the City's main police station, two fire stations, and a library branch. SER291-93. The police station is the command center for the City's police department, and the fire stations, of course, are essential to the City's provision of public safety services. SER358. Needless to say, the City viewed these properties as critical. SER391-92.

The City negotiated with Ambac to reduce the General Fund's maximum obligation on these claims, and to gain needed flexibility in the future to extend payments if necessary. SER358, 553. The City also used certain available restricted tax revenues to repay Ambac, likely relieving the General Fund of significant repayment obligations. SER549-50, 552.

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Franklin, whose bonds were secured by a lease in two golf courses and a park, was the only major creditor with which the City could not reach agreement. But the City's settlement with Assured deliberately left the door open for Franklin. It provided that the contingent funds promised to Assured would be shared pro rata with Franklin if the City and Franklin could come to terms on the treatment of Franklin's claim. SER328-29.

F. The City decides not to impair existing pension obligations in order to preserve its workforce.

Though it cut other compensation and benefits, the City decided to assume its pension obligations (through its contract with CalPERS) in full. ER279. This decision was not taken lightly.

As demonstrated at the confirmation hearing, the potential effects of rejecting the CalPERS contract were seismic. The City could not "trim" its pension obligations and remain in CalPERS—it faced an all-or-nothing choice. SER598. Termination would immediately give rise to an "unfunded termination liability" of $1.6 billion—effectively the amount that, if paid immediately and subject to conservative investment returns, would satisfy all unfunded pension obligations. SER459-60; *see* SER246-49. This massive termination liability would swamp the City's other unsecured claims and, if unpaid, would result in a 60% pro rata cut to existing pensions of both retired and current employees. SER466. Termination would also trigger a priming lien in favor of CalPERS on all City assets. SER460-61; Cal. Gov't Code § 20574.

Equally dire was the potential impact on the City's ability to hire and maintain a qualified workforce. A CalPERS pension, put simply, is the market standard in California. SER396; *see* SER346. "[N]inety-nine percent of government employees in California are in the CalPERS program or something very similar." SER346. Moreover, the portability of CalPERS pensions makes it easy for California municipal employees to move to other CalPERS employers, as well as other public employers such as those with so-called '37 Act pensions. SER598-600.

The City's witnesses explained what impairment would do to the City's viability as an employer. Chief of Police Eric Jones testified that he had spoken with City police officers that "have said they will depart to another agency if the Department's PERS contract is broken," while "[o]thers have stated that they will leave the Department if any additional compensation or benefits cuts occur." SER174. He described exit interviews with officers leaving his department, stating that "[a]ll of the officers told me that monetary issues were the primary reason they were leaving." SER174.

Chief Jones's concerns were not hypothetical; the City was already struggling to recruit and retain qualified officers. As of the confirmation trial, the City had been unable to fill even the 365 funded positions that remained in the budget after several years of cuts, let alone the 120 additional officer positions that were newly funded by a tax increase that had been approved by voters during the chapter 9 case, *infra* 25. SER331-32. From January 2012 through March 2014, 104 police officers had departed Stockton—44 to other police departments. SER332. Given the City's already staggering crime rate, SER239-40, 260 (Eligibility Opinion), it could not risk the loss of additional police officers.

The potential impact was not limited to police. In fact, if the City's CalPERS contract were terminated, most City employees would be strongly incentivized to leave for another CalPERS agency *within six months* in order to avoid being permanently relegated to a lower level of benefits under newly-enacted standards. SER478-86.

The City considered other options, but came to the conclusion that there was no feasible, less costly alternative by which it could provide a competitive pension. SER346, 396. With an alternative pension system, City and CalPERS witnesses explained, would come start-up costs, lower investment returns, increased financial risk, higher required pay-ins, and a loss of portability. SER346, 396, 451, 469-78, 487-88, 498-502, 598-99. Put simply, leaving CalPERS would mean greater costs, smaller pensions, and a likely exodus of employees. The City had no choice but to assume the contract.

G. The first amended plan.

On November 15, 2013, the City filed its first amended plan of adjustment. ER115. It addressed over $1.5 billion in debts spread across (at the time) 19 classes of creditors. SER282-84. The treatment of the vast majority of these creditors reflected the agreements summarized above.

When the City put the first amended plan to a vote in early 2014, all of the City's material creditors but one voted to approve it. SER378-80. Franklin's claim was secured by leases that the City proposed to reject, so it was placed in Class 12 with the claims of other general unsecured creditors. ER280. Its "no" vote was outvoted by the other creditors in Class 12. SER379.

The City had won another crucial vote even before the disclosure statement was approved—it enjoyed the support of the community. The financial projections on which the Plan was based—known as the "Long Range Financial Plan" ("LRFP"), *see infra* 26-28— were premised on the assumption that the electorate would vote to approve Measure A, which would increase the sales tax from 8.25% to 9%. SER322. Forecasts were that the tax would generate $28 million per year to shore up the City's understaffed police force, repay creditors, and pay its bankruptcy expenses. SER322. Based on the prospect of the approval of a plan, the voters approved the new tax in November 2013, albeit by the slimmest of margins at 51.86% in favor. SER339.

H. Franklin litigates its claim through an adversary proceeding.

The first amended plan treated Franklin's $36 million claim as an interest in an unexpired lease of nonresidential property rejected by the City. SER281. Franklin brought an adversary proceeding contending that its claim should instead be treated as a partially secured loan. SER514-22. With the first amended plan moving towards confirmation, the City decided that litigating the issue was not worth the delay and diversion of resources, so it moved for partial judgment in favor of Franklin and decided only to litigate the value of Franklin's security. SER541.

The City's motion had the desired effect. The Court granted it, and held an evidentiary hearing to determine the value of the "collateral" (i.e., possessory interests in the golf courses and park) securing Franklin's bonds. It ultimately set the number at $4,052,000, allowing a Franklin secured claim in that amount. ER304; SER231. Pursuant to § 506(a), the remainder of Franklin's $36,603,626 aggregate claim—$32,551,626—was therefore an unsecured claim.[2]

The City filed a modified plan to create a Class 20 into which Franklin's new secured claim was placed. ER269. Franklin's unsecured deficiency claim continued to be classified in Class 12 with the claims of other general unsecured creditors.

I. The confirmation hearing establishes the financial basis for the Plan.

Franklin objected to the Plan, and in May and June 2014, the Court held five days of evidentiary hearings on confirmation issues. At trial, the

[2] The Bankruptcy Court later determined that an additional $2.1 million in reserve funds was available to pay down Franklin's claim, reducing Franklin's unsecured claim from $32,551,626 to $30,480,190. *Infra* 31-32.

City presented ten live witnesses, and nine through declarations, who explained the City's current fiscal circumstances, its inability to deliver municipal services, its employee agreements, its settlements with the three capital markets creditors, and its decision not to impair pension obligations.

The budgetary forecasts underlying the Plan were the focus of much of the testimony. This was the LRFP, the principal author of which was Robert Leland, a Management Partners consultant with four decades of experience in state and local government finance. SER409.

The purpose of the LRFP was to plot a path from the City's present fiscal circumstances to sustained cash solvency, budget solvency, and service delivery solvency. In developing this model, the City considered "as many contingencies as possible in order to develop the most realistic revenue and expense projections that it could to demonstrate solvency over a prolonged period of time." SER409. And mindful as much of where it came from as where it was headed, the City adopted "revenue and expense projections [that] are conservative relative to the pre-recession magnitude of estimates that got the City into trouble in the first place." SER409; SER563-64. The LRFP thus set forth a meticulous analysis of projected revenues on one side of the ledger, and a detailed set of projections of costs—labor, benefits, City services, repayment of creditors, and so forth—on the other. ER790-827.

In addition to realistic financial projections, the LRFP marked a departure from the City's prior practice regarding reserve funds. It budgeted an unrestricted reserve fund with a target of 16.67% of annual operating expenses (two months' worth) to be built up over 18 years, as well as a $2 million annual contingency. SER412-16, 424-26. In the past, the City aspired to maintain only a 5% "catastrophic reserve" and a 5% "economic contingency/budget uncertainty reserve." SER413. Needless to say, the combined 10% reserve proved an inadequate buffer in a serious downturn. SER575-77. So the City adopted the "Best Practices" recommendation of the Government Finance Officers Association ("GFOA"), which called for a 16.67% reserve. SER413. The $2 million contingency would serve as an additional long-term buffer, permitting the City to gird itself in good times to withstand a prolonged downturn. SER424-26, 582-85.

J. The Bankruptcy Court confirms the Plan.

On October 30, 2014, the Bankruptcy Court overruled all of Franklin's objections and confirmed the Plan. Noting that "it is important to look at this case from the standpoint of the big picture," the Court incorporated the lengthy findings of fact from its eligibility ruling. ER413. The Court then described the operation of the Plan, from employee compensation, to retiree health benefits, to CalPERS, to capital markets creditors. ER414-30.

The Bankruptcy Court undertook a lengthy discussion of CalPERS and the City's decision not to impair pensions. Although it found that a CalPERS contract could be modified in a chapter 9 case, the Court also endorsed the City's reasons for declining to do so, making findings as to the serious practical damage termination of the CalPERS relationship would cause. ER424-27. It recognized that employees and retirees, and not CalPERS, are the true creditors when it comes to pensions. ER422-24. And the Court acknowledged that, given all of the concessions and renegotiations reached over the past several years, reopening the pension issue "as a practical matter … would be difficult to do." ER429.

The Court then marched through each of the statutory confirmation requirements. On the issue of the City's good faith, it rejected Franklin's premise that the Plan did not "affect[] pensions" at all, ER436, and took "particular note of the obviously intensive arms-length negotiations that occurred throughout the course of this case." ER437. It also emphasized that the City's agreement with Assured had left the door open for Franklin to share in any future City prosperity on a pro rata basis. ER437; ER356.

The Court made quick work of Franklin's classification argument as well, finding that Franklin's unsecured deficiency claim was properly classified with claims like the Retiree Health Benefits Claims because all such claims were unsecured. ER437. Within each class, the Plan provided equal treatment. ER434.

Next, the Court rejected Franklin's argument based on § 943(b)(3), finding that all amounts "to be paid" by the City "have been disclosed." ER439, 452-53. The Court found that the § 943(b)(3) "to be paid" language "look[ed] to the future … at payments that are to be made during and under the Plan." ER453-54.

Finally, the Court found that the Plan was in the best interests of creditors. It explained that it had "looked long and hard at the history of this case and the responses that have been made and considered the alternatives," and found that "putting the whole situation back to square one" would "run[] up many more millions of dollars in terms of expenses for the City for what [is] probably not likely very much difference." ER442. The Court concluded that "this Plan … is the best that can be done in terms of the restructuring and adjustments of the debts of the City of Stockton." ER442.

K. The Court resolves the post-trial motions, and the Plan goes effective.

After the Plan was confirmed, the parties made several post-trial motions. Franklin filed a motion to Alter or Amend Findings of Fact and Conclusions of Law. ER176. It maintained that the Court should have reduced the Retiree Health Benefit Claims in the amount of $545 million to a present value of $261.9 million. SER507. The City opposed that motion, ER179, and the Court denied it from the bench, ER181.

The City also filed a motion, based on uncontested facts, premised on the parties' recent re-discovery of a reserve account held by indenture trustee Wells Fargo with over $2 million in funds available to pay Franklin's claim. SER509. The Bankruptcy Court agreed with the City that the funds were available to pay Franklin, thus leaving Franklin with a reduced deficiency claim of approximately $30.5 million, and that Franklin's overall recovery in the case was 17.5%. ER304 (Amended Confirmation Opinion); SER510.

Finally, Franklin moved to stay the confirmation order and delay implementation of the Plan pending this appeal. ER176. The City opposed, ER179, and the Court denied the motion, clearing the way for the City to exit bankruptcy. ER184-85. The Plan went effective on February 25, 2015.

SUMMARY OF ARGUMENT

I.A. The Bankruptcy Court correctly rejected Franklin's argument that its unsecured deficiency claim was not substantially similar to, and should not be classified with, other general unsecured claims in Class 12, under § 1122(b). Franklin's primary argument for separate classification is its assertion that certain Public Facilities Fees ("PFFs") are a separate dedicated source of repayment on its claim. PFFs are not, however, pledged as collateral for Franklin's bonds. Rather, they are legally required to be used for infrastructure projects within the City, and in any event are speculative and currently a trickle. Franklin failed to show that PFFs were dedicated to it or in fact available to pay it. Accordingly, the Bankruptcy

Court did not clearly err in finding Franklin's unsecured claim substantially similar to other general unsecured claims.

B. Franklin's attempt to relitigate the City's decision to separately classify other capital markets creditors is similarly meritless. Both the Bankruptcy Court and the City have considerable discretion in classifying claims. As long as the classification decisions are based on sound business and economic reasons, they are proper.

Franklin fails even to mention, let alone contend with, the mounds of evidence and days of testimony that established the City's economic reasoning for its settlement, treatment, and classification of other capital markets creditors. Those capital markets creditors with secured claims held collateral—like police and fire stations—that was vastly more important to the City than the collateral Franklin held—two golf courses and a park. The City reached unique settlements with those parties on the basis of these business and economic considerations, leaving the creditors with secured claims that were required to be classified separately. Similarly, the City settled with Assured regarding the unsecured POBs based on avoidance of very real litigation risk and as part of a global settlement that included a lease on 400 E. Main, the new City Hall.

C. Franklin's argument that its unsecured deficiency claim is not treated equally with other general unsecured claims under § 1123(a)(4) ignores the provision's plain language. Section 1123(a)(4) requires equal treatment only of claims within a particular class. That is the case here. Franklin's unsecured claim is paid the same percentage as the other claims in Class 12. Franklin's suggestion that the Bankruptcy Court should instead have compared total recoveries for creditors, across claims and classes, is unsupported by statute and is unworkable.

D. The cramdown principles invoked by Franklin have no place here. There was no cramdown. Class 12, in which Franklin's unsecured deficiency claim is properly classified, approved the Plan. Franklin is nothing more than a dissenting creditor in an accepting class. Even if cramdown principles did apply, the City has repeatedly demonstrated the fairness of Franklin's treatment.

II.A. The Bankruptcy Court properly concluded, and certainly did not clearly err in finding, that the Plan is "in the best interests of creditors"—as a whole—"and is feasible," § 943(b)(7). Section 943(b)(7) requires only that the Plan be better than the alternative of dismissal of the chapter 9 case while making a reasonable effort to repay creditors. The requirement of "best interests of creditors," moreover, is necessarily informed by the requirement of "feasib[ility]." Franklin's atextual reading of the statute, turning on what is best for each individual creditor, finds no support whatsoever in the case law, and it would render meaningful chapter 9 relief impossible. As long as the Plan is better than the alternative of dismissal (and Franklin does not even try to contest that dismissal would be disastrous for all) and devotes a reasonable slice of the City's revenues to repayment of creditors generally, it fully satisfies § 943(b)(7).

B. Franklin's fact-bound criticisms of the LRFP and the Plan were rejected by the Bankruptcy Court, and Franklin should not be permitted to relitigate them here. They are also, by and large, both wrong and irrelevant under the proper standard.

Franklin is wrong that the LRFP is unduly conservative in its revenue forecasts. The City established the soundness of the LRFP's projections, and Franklin cannot come close to showing clear error. Franklin oddly complains that the City plans to revise the LRFP as it gains new information. Revise to accommodate new information is precisely what the City *should* do, and is in the best interests of all stakeholders.

Franklin's facile, back-of-the-envelope tally of the funds it says should be available to pay its claim is yet another attempt to undermine the considered judgment of the City's budget experts and the Bankruptcy Court's endorsement of the financial underpinning of the Plan. The funds to which Franklin lays claim are not available to pay Franklin—they are essential to the City's functioning and fiscal health, and thus to a feasible plan. Nor is Franklin correct that PFFs are available to pay it. As explained, the use of PFFs is restricted by state law, and in any event that revenue stream is speculative and currently far below Franklin's unfounded and outdated forecast.

III.A. The finding that the City proposed the Plan in good faith under § 1129(a)(3) was clearly correct, not clearly erroneous. A plan is proposed in good faith where it is consistent with chapter 9's broad remedial purpose of permitting a distressed municipality to adjust its debts and emerge from bankruptcy with a sustainable solvency. From start to finish, the City demonstrated utmost good faith in seeking fair and consensual resolutions with all of its creditors—including Franklin—that permitted the City to get its fiscal house in order. There is no basis to believe that the City would single out Franklin for bad faith treatment.

Indeed, the City always kept Franklin's seat at the bargaining table open by ensuring in its settlement with Assured that Franklin would have the opportunity through settlement to share in contingent future revenues if the City prospered. The City worked for years to cut costs, raise revenues, reform its finances, and repay creditors, and the Bankruptcy Court saw this good faith day in and day out.

B. Franklin's list of "six facts" purporting to show bad faith is simply a rehash of the same issues it litigated and lost. It cannot come close to satisfying the clear error standard.

The argument based on separate classification and alleged gerrymandering fails here for the same reason it does in the classification context: Franklin failed to adduce a shred of evidence suggesting that the City classified creditors as it did for the purpose of rigging the vote. Rather, at all times, the City's decision to separately classify was based on sound business and economic considerations.

Franklin's complaint that other creditors fared better through negotiation and that it fared worse by abandoning negotiations does not show bad faith. It shows why parties negotiate in the first place. Other creditors reduced risk and cost and maximized their recovery, while

Franklin opted to litigate. That it is unhappy with the result of its choice is no basis for accusations of bad faith.

The argument that the City acted in bad faith by not impairing pensions suffers from a familiar flaw: Franklin fails completely to acknowledge a mountain of evidence showing that the City had no choice but to satisfy pension obligations, because impairment would mean termination of the City's relationship with CalPERS, and termination would mean massive liability and a devastating blow to the City's viability as an employer.

Franklin's argument that the City showed bad faith by not paying it from PFFs fails because PFFs are not pledged to it as collateral or even mentioned in any of the bond contracts, and because the evidence shows that there are no PFFs available to pay it anyway.

Franklin's suggestion that the City inflated Retiree Health Benefit Claims to penalize Franklin is based on nothing more than that the City took a legal position on the interpretation of § 502(b) with which Franklin disagrees, but on which the City prevailed before the Bankruptcy Court. Taking a successful legal position is not bad faith. Similarly, there is no merit to Franklin's suggestion that the City took a frivolous position in its adversary proceeding. Contrary to Franklin's assertion, the City's position was not frivolous, and, as the Bankruptcy Court well understood, the City dropped the argument only in order to speed confirmation of the Plan.

IV. The Bankruptcy Court correctly held that § 502(b) does not require discounting of the $545 million Retiree Health Benefit Claims to present value. As the Third Circuit reasoned in *In re Oakwood Homes Corp.*, 449 F.3d 588 (3d Cir. 2006), the plain language of § 502(b) directs a court to "determine the amount of [a] claim," not, as ten other Bankruptcy Code provisions do, a claim's "value, as of" a certain date. That § 502(b) does not require discounting is in line with the overarching principle that the Code accelerates the maturity of future obligations to the petition date. Franklin's attempts to overcome plain language and statutory context by resort to generalized accounting principles or meaningless distinctions between interest-bearing and non-interest-bearing obligations fail, because none of that is relevant to interpreting § 502(b)'s language.

Moreover, § 502(b) contains a list of expressly enumerated exceptions—for example, caps on unmatured interest and future rent—but does not require discounting to present value. Reading into § 502(b) an additional exception requiring discounting to present value would render the explicit exceptions superfluous. And the authorities Franklin cites do not support a contrary result because they rely on non-bankruptcy law, analyze irrelevant § 502(b) exceptions, or are no longer good law.

V. Finally, the Bankruptcy Court correctly held that the text of § 943(b)(3), especially in light of surrounding statutory context, requires disclosure only of prospective fees. Section 943(b)(3) calls only for disclosure of fees "to be paid," in contrast with § 1129(a)(4), which explicitly requires retrospective as well as prospective fee disclosure. Doubtless Congress chose not to require retrospective fee disclosure in chapter 9 because of constitutional concerns regarding interference with state and municipal sovereignty. Chapter 9 does not incorporate §§ 326-30 for the same reason. The Bankruptcy Court properly recognized Congress's decision.

STANDARD OF REVIEW

Franklin's required statement of the standard of review is misleading and incomplete, stating only that the Bankruptcy Court's confirmation order is generally subject to de novo review. OB4.

The Bankruptcy Court's conclusions on questions of law—such as the proper interpretation of the text of § 502(b), *infra* § IV, or § 943(b)(3), *infra*

§ V—are, of course, reviewed *de novo*. *In re Camino Real Landscape Maint. Contractors, Inc.*, 818 F.2d 1503, 1505 (9th Cir. 1987). Franklin's challenges to the Court's factual rulings, however, are subject to clearly erroneous review, including those to the Court's findings in its classification ruling, *infra* § I, *In re Johnston*, 21 F.3d 323, 327 (9th Cir. 1994), its determination that the Plan is in the best interests of creditors, *infra* § II, *In re Arnold & Baker Farms*, 177 B.R. 648, 653 (B.A.P. 9th Cir. 1994), *aff'd*, 85 F.3d 1415 (9th Cir. 1996), and its finding that the Plan was proposed in good faith, *infra* § III, *In re Stolrow's Inc.*, 84 B.R. at 172 . "Where there are two permissible views of the evidence, the factfinder's choice between them cannot be clearly erroneous." *Anderson v. Bessemer City*, 470 U.S. 564, 573-74 (1985) (if the court's fact-bound ruling is "plausible in light of the record viewed in its entirety, the court of appeals may not reverse it even though convinced that had it been sitting as the trier of fact, it would have weighed the evidence differently").

ARGUMENT

I. Franklin's Unsecured Claim Is Properly Classified and Treated Under the Plan.

Franklin objects to the Plan's classification of its deficiency claim in Class 12, which includes the claims of holders of other general unsecured claims. It repeatedly asserts that such classification evidences "unfair discrimination." *E.g.*, OB51. There is nothing discriminatory, unreasonable, or improper in classifying Franklin's secured claim in Class 20 (and paying it 100 cents on the dollar), and then classifying the unsecured deficiency claim along with other general unsecured claims in Class 12. Nor can Franklin complain about equality of treatment within Class 12, because each claim received the same percentage payment. Unable to succeed under a straightforward analysis of classification and treatment of claims, Franklin improperly asks this Court to rewrite the Code to import free-floating cramdown principles that have no application in this context. That invitation should be rejected.

A. Franklin's unsecured deficiency claim was properly classified with substantially similar general unsecured claims.

Franklin maintains that the unsecured portion of its claim was not "substantially similar" to the other general unsecured claims under § 1122(b). Substantial similarity is a question of fact, and nothing Franklin points to would suggest that the Bankruptcy Court's decision was clearly erroneous. *In re Johnston*, 21 F.3d at 327.

Franklin's argument that its deficiency claim is different from other general unsecured claims is premised on an asserted right to have its claim paid "from restricted PFFs." OB56. PFFs "are charges levied on new development to pay for development's fair share of infrastructure needs." SER399; *see* Cal. Gov't Code §§ 66000 *et seq.* When a developer builds new residential units, for example, the City charges it PFFs, which the City is then required to use on public infrastructure projects like roads to ease the increased traffic caused by the development. Franklin lays claim to these fees, then maintains that they are "a third-party source for payment" that "*requires* separate classification." OB56 (emphasis Franklin's) (citing *In re Loop 76, LLC*, 465 B.R. 525, 541 (B.A.P. 9th Cir. 2012)).

This argument fails. Of the two cases Franklin relies upon, one, *In re Loop 76*, 465 B.R. at 541, involved a third-party guarantor legally obligated to repay the debt, and the other, *In re Johnston*, 21 F.3d at 328, involved a third party pledge of collateral for the debt. In contrast, the PFFs are not property belonging to a third party and are not legally obligated to Franklin, which has no security interest in them. The only legally obligated source of repayment for Franklin's claim is the General Fund. The bond indenture explains that, pursuant to the related lease transaction the City used to fund the bonds, "the City will agree to make lease payments … from moneys in its General Fund." SER365. The only reference to PFFs appears on the Official Statement, which says that "[t]he City *expects* that [PFFs] will be sufficient to pay the debt service." ER635 (emphasis added). That forward-looking statement reflected the City's belief at the time that it would have excess PFFs, but it does not give Franklin any legal right to be paid from them. *In re Loop 76* and *In re Johnston* therefore do not help Franklin.

The City is required to use PFFs "to pay for projects to mitigate growth"—that is, to pay for the adverse impacts of a new development (such as increased traffic or needs for additional infrastructure). SER427; *see* Cal. Gov't Code § 66001(a)(3), (b). There are many such infrastructure projects requiring the PFFs—the City's Capital Improvement Program has identified $440 million worth.[3] SER406.

[3] In addition, as a practical matter, funds from PFF collection are highly speculative and currently are just a trickle. Indeed, the City's development and corresponding PFFs have been well below Franklin's self-serving forecast (at OB37) of "tens of millions of dollars." Stephen Chase, the City's Director of the Community Development Department, explained how minimal development in the City has been: "[T]he City has averaged less than 130 units per year over the last five years, and [was] stuck on 64 units [10 months into FY2014]." SER406.

Without any special legal right to PFFs, Franklin's unsecured claim's "legal character or effect as a claim against the debtor's assets" and "the relationship of the claim to [the City's] property" is identical to those of other general unsecured creditors. 7 *Collier on Bankruptcy* ¶ 1122.03[1][a][3] (Alan N. Resnick & Henry J. Sommer eds., 16th ed.) (hereinafter "*Collier*"). And because Franklin, through that claim, has the same interests as those other claimants, it is entirely appropriate that it cast its vote alongside them.

B. The City's decision to separately classify Franklin's unsecured claims from the claims of other capital markets creditors was based on business and economic considerations.

Franklin also complains that other capital markets creditors were not classified with the general unsecured creditors, but instead were put in their own classes and recovered at a higher rate. OB52-56. This argument is likewise without merit.

A claim that is not "substantially similar" to another—for example, because it is secured by collateral—must be classified separately. 7 *Collier* ¶ 1122.03[3][c]. And even where claims are similar, it is well established that "both the proponent of the plan and the court itself have wide latitude in determining whether similar claims may be classified separately." 7 *Collier* ¶ 1122.03[3]; *In re Johnston*, 21 F.3d at 327. As Franklin concedes, OB53, as long as the debtor can point to "a legitimate business or economic reason" for separate classification, such classification is proper. *See In re Barakat*, 99 F.3d 1520, 1526 (9th Cir. 1996).

Whether separate classification is justified is a question of fact, and must be viewed in light of a debtor and court's considerable discretion in matters of classification. *In re Johnston*, 21 F.3d at 327. Here, the Bankruptcy Court neither abused its discretion nor committed clear error in permitting Franklin's unsecured deficiency claim to be classified together with general unsecured claims and separately from other claims. Even a brief review of the reasons for separate classification demonstrates that the City's reasons for classifying claims as it did were unquestionably legitimate.

1. Insofar as Franklin challenges separate classification of Ambac, NPFG, or Assured claims secured by collateral, this argument is a non-starter. Collateral matters, and each of Ambac, NPFG, and Assured asserted a security interest in collateral that was vital to the City's recovery, and far more important to the functioning of the City than the interest held by Franklin. Ambac's collateral included leases of three fire

stations and the City's main police station; NPFG's included leases on the arena and downtown parking garages, both centerpieces of the downtown area, as well as the Stewart Eberhardt Building, already home to several essential services; and Assured's was a lease in 400 E. Main, the City's replacement for City Hall. *Supra* 17-20. Franklin's bonds were secured by a possessory interest in two money-losing golf courses and a park. *Supra* 21.

In light of Ambac, NPFG, and Assured's collateral, business and economic imperatives compelled the City to reach an expeditious resolution of their claims, and the City was able to do so, negotiating unique treatment based on the respective creditors' unique collateral. This left Ambac, NPFG, and Assured's secured claims and security interests fully intact. Those claims, like any claim secured by collateral, are *required* to be separately classified. Indeed, it would be nonsensical to classify, say, NPFG's claim, secured by a possessory interest in an arena and a pledge of restricted tax revenues, with general unsecured claims. To the extent Franklin contends otherwise, its argument flies in the face of basic classification principles.

Franklin's collateral, by contrast, was less important as a business and economic matter to the City, and despite the City's best efforts, the parties could not reach a settlement. Franklin litigated instead, leaving it with a secured claim and an unsecured deficiency claim. Just as Ambac, NPFG, and Assured's secured claims were classified separately, so too was Franklin's secured claim placed in its own class (Class 20), and Franklin received 100 cents on the dollar. Its remaining deficiency claim was then classified with other general unsecured claims, which, as explained above, was entirely correct.

This is all rudimentary. The City's agreements with Ambac, NPFG, and Assured reflected a proper, reasonable business decision in valuing the importance of distinct assets implicated by the claims, and the resulting claims were plainly different, in their legal character and their practical importance, from unsecured claims. Classifying them—and, for that matter, Franklin's secured claim—separately was not only permissible, it was mandatory.

2. The Bankruptcy Court also correctly found that valid legal and business considerations justified separate classification for Assured's unsecured POBs. To begin with, the treatment of the POBs was part of a

global settlement with Assured, which was critical to guaranteeing the City a new home for its City Hall in 400 E. Main. That alone is a sufficient business reason for separate classification.

The POBs also carried unique legal risks in the context of the bankruptcy case. Assured contended that the proceeds of POBs paid to CalPERS to refund pension liabilities do not create new indebtedness, but rather take on the same character and priority of the pension obligations themselves. SER360; *see, e.g.*, *City of Los Angeles v. Teed*, 112 Cal. 319, 327 (1896) (noting that bonds are "only the evidence" of indebtedness, not "new indebtedness"). Complicating matters, the City sought and secured a Superior Court judgment in 2006 finding that the POB debt was the same debt as the pension obligations it went to fund, and thus did not count towards the City's debt ceiling. SER442-45. Assured argued that this barred the City from impairing its POB claims. Although the City disagreed, the size of Assured's claim and the unsettled law surrounding its arguments carried very substantial risk.

The City's agreement with Assured, embodied in the Plan, reflects a business judgment that this risk, if it materialized, would have imposed a possibly insurmountable obstacle to a feasible plan. And, as mentioned, the Plan's treatment of the POBs was part and parcel of the City's global settlement with Assured for both its POBs and secured claim related to 400 E. Main. The Bankruptcy Court understood the City's discretion, in these circumstances, to place Assured's POB claim in its own class under the Plan, and it approved the City's decision. The Court's ruling is well supported and plainly does not amount to clear error.

3. Franklin confronts none of the above. Instead, it rests its argument (at OB53) on a narrow exception to a debtor's discretion to separately classify claims: A debtor may not "classify similar claims differently in order to gerrymander an affirmative vote on a reorganization plan." *In re Barakat*, 99 F.3d at 1525 (internal quotation marks omitted). In other words, a debtor cannot classify a claim in a certain way solely because of the claimholder's support for or opposition to a plan, and absent any legitimate business or economic reason. *Id.* Without grappling with the evidence of sound business judgment underlying the Plan's classification framework, Franklin accuses the City of a "classic gerrymander." OB55. This is empty rhetoric.

The "classic gerrymander" at which the restriction on separate classification is directed is the scenario in which a debtor separately classifies substantially similar claims in order to manufacture the single accepting impaired class required by § 1129(a)(10). In so doing, it isolates the unfriendly creditors whose claims will be the subject of a cramdown under § 1129(b). *In re Johnston*, 140 B.R. 526, 529 (B.A.P. 9th Cir.), *aff'd*, 21 F.3d 323 (9th Cir. 1994). Here, *10* impaired classes have approved the Plan, so there was no motive to gerrymander past § 1129(a)(10) and into cramdown. Cases like this one are a world away from "classic gerrymander" cases. *See In re City of Colo. Springs Creek*, 187 B.R. 683, 688-90 (Bankr. D. Colo. 1995).

In any event, Franklin adduced no evidence that the City's "sole purpose" for classifying Franklin as it did was to gerrymander the vote—as it would have to show in order to prevail, *In re Barakat*, 99 F.3d at 1525-26; *In re Loop 76*, 465 B.R. at 537.[4]

[4] Lacking evidence, the best Franklin can muster is a citation to the "observ[ation]" of "one commentator" that "Stockton clearly engineered its classes to obtain a desirable voting outcome within each class." OB55 (quoting Richard M. Hynes & Steven D. Walt, *Fair and Unfair Discrimination in Municipal Bankruptcy*, 37 Campbell L. Rev. 25, 68 (2014)). The article does not discuss any evidence either. Indeed, it appears to rely for its observation almost exclusively on argument from Franklin's briefing in the bankruptcy case. *Id.* at 68 n.257; *see id.* at 64 nn.233 & 234, 65 nn.235 & 237-42.

C. Franklin's deficiency claim was afforded the "same treatment" consistent with § 1123(a)(4).

Franklin asserts that the Plan violates § 1123(a)(4)'s requirement that it "provide the same treatment for each claim … of a particular class." OB57. That argument is based on a fundamental misreading of the Code.

A "claim" is a "right to payment." § 101(5)(A). A "creditor" is an "entity that has a claim against the debtor." § 101(10)(A). Section 1123(a)(4), the equal treatment provision Franklin invokes, requires only that a plan of adjustment "provide the same treatment for each claim … within a class." It does not mandate the same treatment for each *creditor*. Here, all claims within Class 12 were treated the same. ER434.

This Court should view this article, which Franklin relies on repeatedly, with a jaundiced eye. The authors' major premise is that debtors in chapter 9 cases do not impair retiree benefits because they view employees and retirees as more deserving than general creditors and unable to protect themselves. The vast majority of the article is devoted to knocking down the straw man it sets up. Like Franklin, the authors fail to discuss or even acknowledge the real business and economic reasons underlying the City's decision not to impair pensions. Indeed, the article never mentions the CalPERS retirement system, much less the complexity of the City attempting to modify its pension obligations administered by CalPERS without the probable loss of its employees. Tellingly, the article's primary source, cited 20-some-odd times, is Franklin's own summary objection to confirmation.

Franklin does not dispute that. OB58. Accordingly, there is no violation of § 1123(a)(4).

Franklin's argument seeks to rewrite the statute. It insists that the proper analysis is to compare its claim to the "overall treatment" of the 1,100 retirees whose Retiree Health Benefit Claims are also classified in Class 12. OB58. It says that because these retirees also have pension-based claims, and because, pursuant to a settlement with the Retirees Committee, the Plan does not impair pensions, the retirees in fact receive a higher percentage of "the City's *total* liability" than Franklin receives on its unsecured deficiency claim alone. OB58.

This proposed expansion of § 1123(a)(4) is sweeping. Any time a creditor holds more than one claim, and those claims are separately classified, § 1123(a)(4) would require a Bankruptcy Court to scrutinize whether there is some link between the two claims such that they are "inexorably joined," OB60. This link, it appears, is satisfied any time the two claims "ar[i]se from the *same contract*[]," OB58 (emphasis Franklin's); "are part and parcel of [a] *single obligation*," OB58 (emphasis Franklin's); or are both settled as part of a "package deal," OB59. If there is such a link, per Franklin's approach, the court must then combine the treatment on the two claims and compare the "overall treatment" of the creditor to the treatment of the objecting creditor's claim—all, presumably, as part of ensuring that each "claim" in a "class" is treated equally. Franklin cites no case applying this methodology, and it would lead to arbitrary and absurd results.

The statute should be applied as written. Under the Code, 1,100 retirees each have two separate and distinct interests in payment. One of these is the lifetime health benefits the City itself undertook to pay them. The other is the pension benefits administered by CalPERS, which the 1,100 retirees with health benefits share with the City's other 1,000 retirees and all of its current employees, and which exists pursuant to the City's contract with CalPERS. The claims are as distinct as Franklin's secured and unsecured claim, and there is no reason to treat them otherwise.

None of the authority Franklin cites refutes this. First, it points to § 507(a)(5)'s priority for claims under an "employee benefit plan," OB59, but does not even attempt to explain how a legislative judgment on priorities establishes that various different benefits under an employee benefit plan are somehow treated as a single claim for purposes of classification and treatment. Also misplaced are its citations to *American United Mut. Life Ins. Co. v. City of Avon Park*, 311 U.S. 138, 144-45 (1940), and *In re Adelphia Commc'ns Corp.*, 361 B.R. 337 (S.D.N.Y. 2007). As Franklin acknowledges, *Avon Park* was not only decided before § 1123(a)(4) was enacted, but it also dealt with a plan that paid a particular debtor a bonus for facilitating restructuring. 311 U.S. at 141. That has nothing to do with treating two separate prepetition debts as a single claim for purposes of applying the text of § 1123(a)(4). *In re Adelphia*, too, is a case about an "added benefit … given for … [a] collateral reason[]," and possible "prejudice[] by a quid pro quo," and again the court did not apply § 1123(a)(4). 361 B.R. at 363.

The Bankruptcy Court properly applied the plain language of § 1123(a)(4) to Franklin's treatment under the Plan. Franklin is entitled to no more.

D. Franklin's cramdown argument ignores the fact that there was no cramdown, but in any event Franklin's treatment was entirely fair.

Finally, Franklin engages in a lengthy and irrelevant cramdown analysis. Cramdown applies only where an impaired class does not accept a plan. *See* § 1129(b); § 1129(a)(8). Franklin's claim was not subjected to cramdown because Class 12 accepted the Plan. Franklin "is simply a dissenting creditor in an accepting class," bound by the majority's vote. *In re City of Colo. Springs*, 187 B.R. at 690.

Franklin's brief consumes several pages trying to muddy the Bankruptcy Code's statutory classification framework by dragging cramdown principles into the analysis. OB50-52. It seems to advocate a free-form inquisition into creditors, claims, classes, and treatment, informed only by its own repeated invocations of the specter of "unfair discrimination." *E.g.*, OB 51 ("[T]he appropriateness of classification in a particular case is determined with reference to the Code's prohibition of unfair discrimination."). But whether "discrimination" in the form of separate classification is permissible, or whether disparate treatment of a claim in one class informs the equality of treatment of claims in another, are questions answered by straightforward application of the relevant statutory provisions—that, and not Franklin's unguided analysis, is how the Bankruptcy Code guarantees that all claims receive fair and equitable treatment.

While cramdown principles have no application here, if they were applicable, Franklin's unfair discrimination argument would still fail under the four-part test articulated in *In re Ambanc La Mesa Ltd. P'Ship*, 115 F.3d 650, 656 (9th Cir. 1997). Its putative showing on those factors—(1) a reasonable basis for differential treatment; (2) the necessity of differential treatment to confirming a plan; (3) good faith; and (4) a rational relationship between the differential treatment and its justification—consists of the same debunked arguments Franklin raises on classification and other challenges in its brief.[5] We have explained above (at 42-51) why Franklin's deficiency claim was classified and treated differently from others. And we explain below (at 65-68, 70-73) why that treatment was essential to a feasible plan of adjustment and (at 76-88) why the Bankruptcy Court was right to find that the City proceeded in good faith

[5] Franklin's one new point is the half-hearted suggestion that the City's decision not to impair pensions was based on "sympath[y]" for the former employees. OB65-66. This ignores the City's massive cuts to compensation pre-filing; elimination of employee health benefits; indirect reductions to pensions; and elimination of lifetime Retiree Health Benefit Claims. *Supra* 8-9, 17. And, as discussed (at 21-24), the decision to assume the CalPERS contract and leave the pensions intact was an economic one that Franklin does not even challenge on the applicable statute, § 365(a), which permits a debtor to assume a contract as long as the decision satisfies the business judgment rule, *In re Pomona Valley Med. Grp., Inc.*, 476 F.3d 665, 669-70 (9th Cir. 2007).

throughout the chapter 9 case. Cramdown analysis has no place in this case—but if it were relevant, Franklin would be sunk on that issue, too.

II. The Bankruptcy Court Did Not Clearly Err in Finding the Plan to Be in the Best Interests of Creditors and Feasible.

Franklin challenges the Bankruptcy Court's finding that the Plan is "in the best interests of creditors and is feasible," § 943(b)(7). A court's judgment that a plan of adjustment satisfies this standard presents a question of fact reviewed for clear error. *See In re Arnold & Baker Farms*, 177 B.R. at 653. Implicitly recognizing that it cannot even come close to showing clear error in the Bankruptcy Court's factual finding, Franklin tries to argue that the Court applied the wrong legal standard. OB28-32. It ignores that a plan must be feasible and in the best interests of the "creditors" plural, and argues that a plan cannot be in the "best interests of creditors" if any particular creditor can show that it may have fared better in some alternate universe, never mind what happens to the City or to anyone else. That is not the standard. Indeed, if it were, obtaining meaningful relief under chapter 9 would be virtually impossible because any incentive for settlement would vanish. What creditor would compromise knowing that whatever it left on the table would be vacuumed up by the holdout that did not?

A. The Plan makes a reasonable effort to repay creditors while providing a feasible path to restoring the City's viability.

1. The Bankruptcy Court applied the proper legal standard in finding that the Plan is in the best interests of creditors and is feasible.

a. Section 943(b)(7) requires that a plan of adjustment be "in the best interests of creditors and feasible." As the statutory language makes plain, the creditors' best interests are not viewed in isolation; rather, that concept is "necessarily constrained" by the requirement that the plan provide a feasible path to recovery and stability. *In re City of Detroit, Mich. ("Detroit")*, 524 B.R. 147, 219 (Bankr. E.D. Mich. 2014); *see In re Mount Carbon Metro Dist.*, 242 B.R. 18, 34 (Bankr. D. Colo. 1999). A municipality can therefore "obtain confirmation of a plan, over objection, which does not utilize all of the assets of the estate to retire its obligations." *In re Sanitary & Improvement Dist., No. 7*, 98 B.R. 970, 974 (Bankr. D. Neb. 1989); *see also Detroit*, 524 B.R. at 219 ("[I]f a city 'gives away' too much under a plan, its future ability to fund its plan obligations and daily operations is lessened.").

The best interests of creditors inquiry looks at the interests of "creditors" as a group, *Detroit*, 524 B.R. at 216-17, determining whether, in the judgment of the court, a feasible plan of adjustment provides "a better alternative for creditors than what they already have." *In re Mount Carbon*, 242 B.R. at 34; *In re Pierce Cnty. Hous. Auth.*, 414 B.R. 702, 718 (Bankr. W.D. Wa. 2009); *Detroit*, 524 B.R. at 213; *In re Sanitary & Improvement Dist.*, 98 B.R. at 975; *see* 6 *Collier* ¶ 943.03[7][a]. In the chapter 11 context, that means looking at how the creditors would fare if the debtor's assets were liquidated and distributed under chapter 7. 6 *Collier* ¶ 943.03[7][a]. But § 1129(a)(7) does not apply in chapter 9, and unlike chapter 11, "[c]hapter 9 makes no provision for conversion of the case to another chapter or for involuntary liquidation of any of the debtor's assets." *In re City of Desert Hot Springs*, 339 F.3d 782, 789 (9th Cir. 2003); *see Detroit*, 524 B.R. at 212; 6 *Collier* ¶ 943.03[7][a].

The only "alternative" to chapter 9 is dismissal of the case altogether, leaving creditors to race separately to state courts. *In re Mount Carbon*, 242 B.R. at 34 ("Since creditors cannot propose a plan; cannot convert to Chapter 7; cannot have a trustee appointed; and cannot force sale of municipal assets under state law, their only alternative to a debtor's plan is dismissal."); 6 *Collier* ¶ 943.03[7][a]. This, of course, would ordinarily "result [in] chaos," *id.*, and not serve the best interests of anyone. *In re*

Mount Carbon, 242 B.R. at 34 (requirement that plan provide a better alternative than dismissal is "often easy to establish").

This does not necessarily mean that any plan will be sufficient. A plan must demonstrate "a reasonable effort at payment of creditors by the municipal debtor." *In re Pierce Cnty.*, 414 B.R. at 718. But, as the term "reasonable effort" suggests, the bar is not high. While a "plan that makes little or no effort to repay creditors" at all "may not be in the best interests of creditors," there is no requirement that "the municipality … devote all resources available to the repayment of creditors." 6 *Collier* ¶ 943.03[7][a]. Again, the plan must be feasible. The "debtor must retain sufficient funds with which to operate and to make necessary improvements in and to maintain its facilities." *Id.*

The Court here properly applied this standard. After over two years of litigation, numerous briefs and hearings (including three-day eligibility and five-day confirmation hearings), and a review of the treatment of the various classes of creditors, the Court properly found that the Plan here was both feasible and in the best interests of the creditors. ER441-42.

b. Franklin urges this Court to adopt a different legal standard, asking it to forgo a collective examination of the creditors' best interests.

OB27. It argues that a court instead must undertake a best interests "inquiry [that] is specific to each dissenting creditor." OB27-28. Under this reading, before the Court could confirm the Plan, § 943(b)(7) required it to review every single non-consenting creditor and specifically ask, "Is this Plan in the best interests of Franklin?" "Is this Plan in the best interests of each of the 13 out of 1,100 retirees who voted against it?" "Is this Plan in the best interests of each non-consenting Class 14 tort creditor?" And since § 943(b)(7)'s text makes no distinction between consenting and non-consenting creditors, Franklin's reading would seem to require this inquiry for *every* creditor, regardless of its vote on the plan.

No court has ever taken that approach. Indeed, in *Detroit*, the bankruptcy court specifically rejected the notion that a plan of adjustment is not in the best interests of creditors simply because one individual creditor "could theoretically receive a better recovery if the case were dismissed." *Detroit*, 524 B.R. at 216. "The plain language of [§ 943(b)(7)] compels" an analysis that looks to "the best interests of the creditors as a whole." *Id.* at 217.

In arguing for its one creditor at a time approach, Franklin cites authorities stating that § 943(b)(7) "*is designed to protect the dissenting* *minority of a class that has accepted the plan*." OB30 (citing 6 *Collier* ¶ 943.03[7][a]) (emphasis Franklin's). The proposition is based on a statement in *Kelley v. Everglades Drainage District* that the "fact that the vast majority of security holders may have approved a plan is not the test of whether that plan satisfies the statutory standard," 319 U.S. 415, 419 (1943). But the statement in *Kelley* stands for no more than that a dissenting creditor like Franklin can raise a best interests objection (as it does now) even when the requisite majority of the other creditors in its class have approved the Plan. The ultimate test remains a holistic one—whether the creditors viewed collectively are better off than if there were no plan at all and the case was dismissed. It does not follow from the fact that an individual creditor can raise a § 943(b)(7) objection that the legal standard requires individualized analysis.

Franklin also argues that a historical link to § 1129(a)(7) requires reading § 943(b)(7) as focused on each individual creditor's best interests. OB29-30. It ignores dispositive textual differences between these sections. Section 1129(a)(7) explicitly requires that "each holder of a claim … will receive or retain under the plan … value … that is not less than the amount that such holder would so receive or retain if the debtor were liquidated." Section 943(b)(7), by contrast, does not refer to individual holders of claims and says only that a plan "must be in the best interests of creditors and … feasible," words nowhere to be found in § 1129(a)(7). Congress could have required § 943(b)(7) to evaluate "each holder of a claim," but it did not. Rather, § 943(b)(7) unmistakably speaks to the best interests of "creditors," plural. *Detroit*, 524 B.R. at 216-17. That difference cannot be simply ignored or wished away by Franklin.

Ultimately, what Franklin seems to be after is a best interests standard that prescribes myopic scrutiny of each creditor's treatment under a plan of adjustment, and the maximizing of each creditor's recovery from the debtor's limited assets. But § 943(b)(7) does not contemplate fine-grained adjustments to recoveries that leave some creditors' interests enhanced and others' decreased, while milking every last dollar from a distressed municipality. The twin components of § 943(b)(7)—feasibility and best interests—call only for an analysis of the total size of a municipality's future pie, and a finding that the rough sizes of the slices allocated to the municipality and creditors reasonably ensure both a functioning municipality and a better state of affairs for creditors than the alternative—dismissal of the case.

The proper standard is what the text of § 943(b)(7) and every relevant authority says it is. Is the Plan better than the alternative of dismissal while making a reasonable effort to repay creditors as a whole? If so, then it passes muster.

2. The City demonstrated that the alternative to the Plan—dismissal of the chapter 9 case—would be disastrous, and that the Plan reflects a "reasonable effort" to repay creditors.

On appeal, Franklin tries to avoid the key question of whether the alternative of dismissal would be better than the proposed plan. Instead, Franklin wants to examine how every dollar not given to another creditor and left to help keep the City from insolvency could instead line Franklin's pockets. The focus, however, is properly on what the state of affairs would be without any plan. Under that standard, the Bankruptcy Court's ruling must be affirmed.

The Bankruptcy Court was keenly aware of the great perils of dismissal. SER265 (Eligibility Opinion). Thousands of creditors—Franklin, the other capital markets creditors, retirees, employees—would all race to state court. This would do them little good because the City could not hope to pay their judgments without the benefits of the Plan to lift it into sustainable solvency. And even if the City had those assets, they would be subject to CalPERS' $1.6 billion statutory priming termination lien. *Supra* 21. Amidst all the financial chaos, employees would leave, vendors would stop offering goods and services, recourse to the credit markets would evaporate, crime rates would rise, and the tax base would melt away, all leading to a downward spiral towards the City's ultimate collapse. That is not in the interests of the creditors, whether viewed collectively or individually.

The Bankruptcy Court correctly understood that the Plan represents a more than "reasonable effort" to repay creditors, recognizing that it, in substantial part, is the embodiment of a series of mediated agreements, the result of "obviously intensive arms-length negotiations" with numerous creditors. ER437. All sides made "significant concessions." ER437. The City's voters raised taxes on themselves to a rate that is among the highest in the state, and the Bankruptcy Court heard testimony explaining why raising taxes even higher was a non-starter. SER340-41. The resulting Plan provides for the creditors while enabling the City to restore its police and fire departments to acceptable levels, rejuvenate its business district, and replenish depleted reserves over time so as to mitigate the risk of future insolvency.

The LRFP proves it. Franklin lobs various specific accusations at the LRFP, arguments we dispatch *infra* 68-73, but its challenge to the reasonableness of the LRFP's treatment of creditors as a whole is outlandish. The LRFP tugs the City's belt tight. Under its projections, the police department will operate 100 sworn officers short of recommended levels indefinitely. SER332. The LRFP also leaves the City at or near service delivery insolvency with respect to libraries, administrative support, and recreation. SER586. It puts off for two decades other "mission critical" expenses, such as millions of dollars per year in deferred maintenance. ER655; SER568-70. And the City does not expect to be operating with the reserve level recommended by the GFOA until FY2033-34. SER426. As the Deputy City Manager testified, "[t]he City has cut every expense that it can while remaining a viable City." SER371.

The Court had a thorough understanding of this. Franklin plucks out the Court's final words on the Plan's efforts at repayment from the confirmation hearing and denigrates them as "*the Court's* _*entire*_ *legal analysis*."[6] OB26-27 (emphasis Franklin's). This ignores the lengthy trials

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[6] Franklin does not challenge the adequacy of the court's findings, nor could it at this point because it waived that argument below. *Hollinger v. U.S.*,

on eligibility and confirmation; the extensive factual findings from the eligibility stage, meticulously detailing the City's financial condition, which the Court incorporated into its confirmation decision; the seven briefs and numerous hearings through which the parties crystallized the pertinent issues; and the sum total of the Court's extensive experience and perspective gained from living with this case and its issues over two years. The Court properly concluded that the City's efforts were beyond reasonable, and in fact "the best that can be done in terms of the restructuring and adjustments of the debts of the City of Stockton." ER442.

B. Franklin's attacks on the Plan and its financial underpinning are without merit.

1. The critiques of the LRFP are factually incorrect and plainly inadequate to show that the Plan's effort to repay creditors is unreasonable.

The only financial forecasting evidence in this case was supplied by the City in the form of the LRFP. Franklin's budget expert conceded that he did not undertake an alternative model and did not take issue with any

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651 F.2d 636, 640-41 (9th Cir. 1981) (a party that "fail[s] to move the district court to amend its findings or make additional findings" "cannot [on appeal] complain of the lack of specificity in the finding").

of the City's numbers. SER591-93. Franklin was content with an all-or-nothing trial strategy of depicting the LRFP as an attempt to hide money from creditors. The Court was thus left with a binary choice, and after hearing all of the evidence properly rejected Franklin's attacks. Franklin's effort to relitigate its rejected arguments here fares no better.

"Conservative Forecast." Perhaps Franklin's most baffling critique is its complaint that the LRFP's "revenue and expense projections are conservative," ER790. *E.g.*, OB18-19. There is an obvious incongruity in a creditor advising a bankrupt municipality to throw caution to the wind. Leland explained that that sort of thinking is what "got the City into trouble in the first place." SER409.

Leland also amply demonstrated why the revenue projections are realistic and why Franklin's simplistic objections are wrong. For example, Franklin's expert argued that Leland should not have forecast the City's compound annual growth rate as lower than the actual rate for the 15-year period preceding the chapter 9 case. SER420. Leland refuted this suggestion, explaining why the "dramatic rise and fall in revenues" during this period risked an unrealistic projection. SER420. He also explained his own "forward looking property tax forecast model," relying on "the four major elements of property tax growth and develop[ing] separate growth estimates for each one of these elements." SER421.

"Living Document." Similarly strange are Franklin's digs at Leland's description of the LRFP as a "living document," ER652, based on a forecasting model that could be "improve[d]" "as inspiration strikes," ER659. OB35, 39. Leland explained what he meant: "It's not a static set of numbers that remain immutable over time. We're constantly getting new information, and as that comes in, we will periodically update. That's what you want the City to do, is respond to changing circumstances over time." ER652-53. Improving its forecasting and adapting to new information is precisely what the City should be doing.

"Hoarding Cash." Franklin next argues that the City "*is actually hoarding cash in its LRFP*." OB36 (emphasis Franklin's). In its Statement of the Case, Franklin purports to tally up what it says is the City's "ability to pay." OB17. Its calculations are deeply misleading.

Franklin begins by attacking the reserves. It asserts that in FY2040-41 the City will have accumulated $58 million in general reserves and $56 million in contingency reserves, and it contends that this means "$114 million potentially available to pay Franklin." OB19. Franklin does not specifically challenge the necessity of a $2 million contingent reserve on appeal, nor could it, because the City explained exactly why the LRFP depends on it "as a long-term buffer against natural swings in economic conditions." SER414 (emphasis omitted). Leland, the architect of the LRFP, explained that in his experience such a reserve is "common." SER584-85.

As for the general reserves, Franklin maintains that the City should not have budgeted 16.67% of annual operating costs as its target reserve level "when 10% is consistent with the City's stated recommended policy." OB36 (quoting its expert, ER606). This is easily answered. The last time the City's "stated recommended policy" prescribed a 10% general reserve was the June 2010 annual budget for FY2010-11. SER413. Leland testified that "as the City's financial health began to deteriorate," it realized 10% was "inadequate." SER413. So the LRFP adopted the 16.67% benchmark recommended by the GFOA. SER413; *supra* 28. That is not unreasonable, it is prudent.

Next, Franklin comes after the City's "mission critical" expenses, calling them a "plug number" and complaining that "[t]he City never itemized" them "much less prepared a budget forecast [for] them." OB35-

36. It is not at all a "plug number." The way the "mission critical" budget works is that after the City finally reaches its reserve level—projected to be FY2033-34, SER426—it begins to devote funds to unmet operating expenses and deferred maintenance. SER569-70. Leland testified to a "daunting array of needs"—the shortage of police officers, outdated accounting system, deferred maintenance, and library, administrative, and recreational expenses discussed above (at 8-10, 67). The LRFP does not put specific numbers on what these costs will be because the City cannot know precisely what these needs will be in *19 years* when the City projects it will be able to address them. But "[d]elusive exactness of findings is … not demanded." *Kelley*, 319 U.S. at 419.

Finally, Franklin argues that the $2.7 million in annual subsidies the City devotes collectively to the Stockton Arena, Bob Hope Theater, Oak Park Ice Arena, and its minor league baseball stadium could be used to pay Franklin. OB19-20. Leland explained why the subsidies are so vital to the City's recovery: "These facilities are important to the economic vitality and quality of life for residents. There cannot be a long-term recovery if the community does not offer some amenities to its residents." SER429. *See Detroit*, 524 B.R. at 218 (reasoning that the Detroit Institute of Arts is "critical … to feasibility," because it supports "values" needed to "uplift, inspire, and enrich [Detroit] residents and … visitors" as well as "attract new residents, visitors, and businesses").

The complaints about "hoarding cash" end with the statement that "the City surely had the ability to wring more than $285,000"—the payment on Franklin's unsecured deficiency claim—"out of the 'living' Long-Range Financial Plan over the next thirty years had it so desired." OB39. This statement reveals Franklin's deep misunderstanding of the best interests of creditors standard. Could the City reduce its police force from 485 to 475 officers to "wring" more money out of the LRFP, or devote less to its reserves and hope it does not face another deep downturn? Perhaps. But that is not required. The plan must be feasible for the City and reasonable toward creditors based on sound budget projections for a sustainable fiscal condition.

2. Franklin is incorrect that PFFs must be made available to pay Franklin.

Franklin next turns to what it says are "tens of millions of dollars of restricted [PFFs]" that it asserts are "available to pay Franklin's claim[s]." OB37. As we explained *supra* 43-44, Franklin is wrong. To begin with, the use of PFFs is legally circumscribed, limiting the City's ability to use them to pay Franklin. Projections of future PFFs, moreover, are highly speculative. As Stephen Chase, the City's Director of Community Development, explained, "[t]he City … has no control over the timing or amount of PFF revenues." SER401.

At the confirmation trial, the Bankruptcy Court heard Chase refute the same argument Franklin advances here. Chase explained that Franklin's suggestion that PFFs would be available to pay it had no basis in fact. SER400-05. He detailed how the City's once sanguine projections regarding development and PFFs—upon which Franklin's estimate relies—did not pan out. SER402-03. As Chase put it, Franklin's assertions regarding PFFs are "a world away from Stockton's reality." SER404. PFFs simply are not available (or legally obligated) to pay Franklin, so the fact that the Plan does not require the City to use them to pay Franklin does not violate the best interests standard.

3. Franklin's other contentions are completely irrelevant to the best interests of creditors requirement.

Finally, Franklin recites a list of gripes with the Court's understanding of how the Plan treats various creditors and claims. OB39-50. It says that the Court improperly "[l]umped [t]ogether" Franklin's secured and unsecured claims to assess its overall treatment. OB39. It contests the Court's comparison of Franklin's treatment to other capital markets creditors, OB43, and its description of the terms of the City's settlement with capital markets creditors, employees, and retirees, OB44-45, 45-48. And it takes issue with a few stray remarks that it says "apparently impacted" the Court's conclusion, while offering nothing to support that notion. OB48.

For purposes of § 943(b)(7), those complaints are simply irrelevant. The best interests requirement does not turn on individualized treatment of creditors, *supra* 61-65, so Franklin's argument that the Court improperly "lumped together" its secured and unsecured claims is beside the point. Indeed, the very statement by the Bankruptcy Court with which Franklin takes issue explicitly applied to "the legitimacy of classification … or the good faith of the plan proponent," ER357, not best interests. OB39. In any event, there is nothing inherently wrong with acknowledging a creditor's overall treatment—Franklin itself does it, OB58 (discussing retirees' "overall treatment"), and the Bankruptcy Court did so only in response to Franklin's misleading comparison of its unsecured claims with the "overall treatment" of other creditors with claims in its class, *see supra* 52-55.

Neither does the best interests requirement entail an inquiry into whether the plan is "fair and equitable." 6 *Collier* ¶ 943.03[7][a]. So how could it possibly be relevant that "the Plan provided a recovery of 52% on the Pension Obligation Bonds," OB44? Section 943(b)(7) simply is not about relative treatment of individual creditors. The best interests requirement is satisfied so long as the Plan is better than the alternative and is reasonable.

III. The Bankruptcy Court's Finding That the Plan Was Proposed in Good Faith Was Not Clearly Erroneous.

Franklin challenges the Bankruptcy Court's finding that the Plan was proposed in good faith under § 1129(a)(3), repeatedly referring to the Plan as "punitive" and "discriminatory," and alleging that the City intentionally "bludgeoned Franklin." OB76-78. The Bankruptcy Court saw the City's good faith day in and day out, and its finding that the City acted in good faith in every facet of the case is correct, and thus not clearly erroneous. *See In re Stolrow's Inc.*, 84 B.R. 167, 172 (B.A.P. 9th Cir. 1988) ("The bankruptcy judge is in the best position to assess the good faith of the parties."); *see also In re Corey*, 892 F.2d 829, 835 (9th Cir. 1989) (granting "substantial deference" to the court's finding of good faith).

A. The Bankruptcy Court correctly held that the City's earnest efforts to negotiate a consensual plan and put its fiscal house in order show the City's good faith.

A plan is proposed in good faith where it is "intended to achieve a result consistent with the objectives of the Bankruptcy Code." *In re Corey*, 892 F.2d at 835. The Bankruptcy Court well understood chapter 9's "broad remedial purpose," SER270 (Eligibility Opinion)—permitting a distressed municipality to restructure and emerge with sustainable service delivery solvency, 6 *Collier* ¶ 901.01[1]—and had little trouble concluding that the City's efforts were at all times consistent with it.

1. The City has slashed costs, imposed new taxes, and otherwise done everything it could to propose a plan that pays creditors fairly while ensuring that the City would emerge from bankruptcy on stable financial footing. Before filing its bankruptcy case, the City cut its workforce by a quarter, slashed compensation by as much as 23%, and negotiated new CBAs. SER169; *see* SER16, 182-83, 238 (Eligibility Opinion).[7]

[7] Franklin repeats its complaint that the concessions made by the City's employees "merely reduced 'above market' pay and benefits to a 'market' level." OB46. Surely paying employees market rates does not constitute bad faith. In any event, Franklin completely disregards the impact on employees that were laid off, whose compensation was reduced to nothing.

The City also worked diligently to increase revenues, culminating in Measure A, the tax increase that will raise approximately $28 million per year to improve police services and fund payments to creditors under the Plan. ER420 ("[I]ndeed, it's the projected tax revenues from [the new tax] that provided the funds that enable the City of Stockton to be able to pay what is proposed under the Plan.").

The City's good faith, as the Bankruptcy Court found, extended to its negotiations with its various creditors. From the outset, "[t]he fact that pre-filing agreements were reached to modify all unexpired collective bargaining agreements, and that substantial progress was made regarding expired agreements that were resolved soon after the chapter 9 case was filed, persuasively testifie[d] to the City's good faith negotiations." SER249 (Eligibility Opinion). The City then engaged in "obviously intensive arms-length negotiations … throughout the course of this case," ER437, resulting in mediated settlements with all of its other significant creditors, including the other capital market creditors, two of whom were bitter opponents during the eligibility phase.

2. The Bankruptcy Court put the fairness and propriety of these agreements, along with that of the Plan generally, on trial during the

confirmation process—what it called "the day of reckoning." SER166 (Rule 9019 Opinion). The City provided extensive justification through a stack of declarations and days of testimony explaining the good faith and fairness of its agreements with and treatment of its various creditors, and Franklin refutes none of it.

As detailed *supra* 16-20, the City's agreements furthered two key goals. The first was to preserve crucial assets for City use. Through its agreements with Ambac, NPFG, and Assured, the City was able to ensure that three fire stations, a police station, a library branch, the downtown arena and parking facilities, the Stewart Eberhardt Building, and 400 E. Main—all of which serve quintessential municipal functions—would remain available to it.

The second major goal was to relieve the General Fund. Again, the City succeeded. The restructuring of Ambac's certificates of participation, for example, is likely to permit other available revenue sources to cover the entire repayment obligation, relieving the General Fund completely, and the City also negotiated a cap on General Fund exposure just in case. The City obtained similar relief by restructuring NPFG's arena bonds and transferring City parking facilities to the Parking Authority, and by negotiating with Assured for a below-market lease in 400 E. Main and a huge reduction in repayment obligations for the POBs.

Finally, the City negotiated comprehensive agreements with its unions and the Retirees Committee that dramatically reduced General Fund obligations going forward, while preserving the City's viability as an employer and service provider. The deals with the unions reduced compensation to at or below market levels and, among other things, reined in future pension obligations indirectly by increasing employee contribution requirements. The agreement with the Retirees Committee eliminated $545 million in retiree health benefits for a lump-sum payment of $5.1 million. Meanwhile, pursuant to its new CBAs, SER556-57, and agreement with the Retirees Committee, the City agreed to assume its obligation to fund the pensions of its many current and former employees, a crucial component because it guaranteed that the City would emerge from bankruptcy as a viable employer.

3. In the face of fair and consensual adjustments of some $1.5 billion in debt, Franklin suggests that the City singled out its $36 million claim for bad faith treatment. That is baseless, because the City hoped to settle with Franklin as well, and its contingent settlement with Assured left open the

possibility for Franklin to share in up to 22% of the contingent payments. *Supra* 21.

But Franklin chose to litigate and hope for a high valuation of its collateral, which was simply less valuable to the City's recovery than that of the other capital markets creditors.[8] From start to finish the City treated all creditors fairly in seeking a consensual plan. When it could not come to terms with Franklin, it proposed a plan that paid Franklin 100 cents on the dollar on its secured claim and more than $6 million in toto under the approved Plan—a 17.5% recovery. That hardly bespeaks bad faith or punitive behavior.

B. Franklin does not come close to showing that the finding of good faith was clear error.

Franklin lists "six facts" it says "collectively demonstrate bad faith toward Franklin." OB76-77. The asserted "facts" are just reruns of

[8] Franklin says "there is no evidence of the value of collateral held by other bondholders" and that "Standard & Poor's gave the City's other lease revenue bonds the *same underlying rating* as Franklin's bonds." OB43-44 (emphasis Franklin's); *see* OB10, 65, 79. The City, however, amply explained the business and economic reasons behind its classification decisions. As for Standard & Poor's bond ratings, as Franklin concedes, they do nothing more than indicate "prospects of recovery." OB44. They have no bearing on the business and economic decisions the City must make regarding collateral that serves critical City functions.

rejected arguments that do not move the needle under the clear error standard.

Gerrymandering. Franklin says it is a "fact" that the City "gerrymandered" the Plan to harm Franklin. As discussed *supra* 42-51, the classification of Franklin's claim was based on the rudimentary principle that general unsecured claims are classified together, while the classification of other claims was based on fundamental legal distinctions, sound business rationale, and the City's ability to reach global settlements with several creditors.

Negotiations. Franklin argues that the City acted in bad faith because it "improved recoveries for all other creditors from those proposed in the pre-bankruptcy Ask, while dramatically reducing Franklin's recovery from what had been offered before bankruptcy." OB77. That other creditors were able to negotiate somewhat better resolutions than the City initially offered in the AB 506 process hardly evidences bad faith. On the contrary, it indicates that the City was never in the take-it-or-leave-it mindset Franklin accuses it of (at OB14), and at all times negotiated in good faith.

As for the fact that Franklin was ultimately paid less than the City's initial proposal would have provided, that just shows why parties often settle, rather than litigate. Parties come to the negotiating table to mitigate risks and avoid the costs and delays of litigation. When they sit down to negotiate, they may not know the amount of a claim, whether a valid security interest exists, or the value the bankruptcy court will place on collateral. The mediated negotiations took those risks into account and achieved carefully-crafted, mutually acceptable resolutions. If a party walks away from the bargaining table, it takes a considered gamble, namely, that it will do better, not worse, than the offer it rejects.

Here, Franklin decided to pursue litigation and the Bankruptcy Court found that its security interest was valued at $4 million, and not the $15 million Franklin asserted. Having achieved less than it had hoped through litigation, Franklin cannot now cry bad faith that it was not given what the City offered when the City was trying to avoid the risks and burdens of litigation.

Pensions. Franklin renews its complaint that the City did not impair pensions in order to provide Franklin with a greater recovery. As already noted (at 57 n.5), Franklin does not even challenge the pension decision under § 365(a) or the applicable standard—the decision must be "so manifestly unreasonable that it could not be based on sound business judgment, but only on bad faith, or whim, or caprice," *In re Pomona Valley Med. Grp., Inc.*, 476 F.3d at 669-70. Nor, more importantly, does it ever mention, let alone confront the extensive evidence the City proffered explaining why its only option was to fully fund pensions, including testimony by two City Managers, the Chief of Police, the Human Resources Director, and the City's pension expert, in addition to the testimony of the CalPERS Deputy Chief Actuary. *Supra* 21-24.

Franklin also ignores the finding that the City took several important steps to *indirectly* reduce pensions, through lower compensation, implementation of new pension tiers, and requiring employees to pay a larger portion of their pension costs. ER436; *see* ER414-15; SER389, 416-18, 436-38. As the Bankruptcy Court recognized, "renegotiated collective bargaining agreements providing for reduced compensation indirectly reduce the City's CalPERS obligations." SER250 (Eligibility Opinion).

Future Revenue. Franklin reiterates its complaint that "the City failed to apply any future revenues (including PFFs) to repayment of Franklin's claim." OB76. As described in detail above (at 70-73), the projected future revenues Franklin seeks for itself are in part what makes the Plan feasible—they restore basic City services and establish fiscal safeguards against future insolvency. There would be no feasible plan if they were instead used to pay Franklin or other creditors. Moreover, as explained *supra* 43-44, 73, the evidence presented at the confirmation hearing showed that PFF revenues had slowed to a trickle, were possibly insufficient even to cover the infrastructure needs for which they were legally required, and were unlikely to increase substantially going forward. SER400-04.

Franklin also asserts that "the City admitted it would be 'a sign of bad faith' if PFFs were not used to pay Franklin." OB76. That is a brazen misrepresentation of the record. The staff report Franklin cites actually says that "[t]he City cannot *forgo the collection* of the [PFFs] .... To do so would be seen as a sign of bad faith by the Bankruptcy Court and creditors." ER836 (emphasis added). The City was saying that it should not reduce the fee requirements in light of its bankruptcy. It did *not* say that it would be bad faith not to devote those PFFs to Franklin.

Retiree Health Claims. Franklin asserts that the City "inflated retiree health benefit claims for no reason other than to reduce the distribution on Franklin's unsecured claim." OB76. In other words, the City is accused of bad faith for taking the legal position discussed *infra* § IV, that § 502(b) does not require discounting to present value. On appeal, Franklin renews its argument, but it cannot be said that simply by taking a position (that the Bankruptcy Court deemed correct), the City acted in bad faith.

Lease/Lease Back Argument. Finally, Franklin argues that the City showed its bad faith by "frivolously assert[ing] that Franklin's claim should be capped pursuant to section 502(b)(6) of the Code." OB77. This is a reference to the City's initial position in the case and in the adversary proceeding that Franklin's claim was properly capped as a claim for rent on an unexpired lease.

For reasons having to do with municipal bond issuance restrictions under California state law, the bonds that Franklin purchased were tied to a "lease/lease back transaction." In essence, City property is leased out to a conduit—the City's Public Financing Authority—and then back to the City, and the City's lease payments are used to repay the bonds. SER514-19. Under the first amended plan, the City proposed to treat Franklin's claim as precisely what it is under state law: one arising under an unexpired lease of nonresidential real property. Indeed, it is well-settled that bankruptcy courts must look to state law to characterize a transaction. *In re Fitness Holdings Int'l*, 714 F.3d 1141, 1146 (9th Cir. 2013). The Bankruptcy Code permits a debtor to reject such leases, § 365(a), and limits allowance of a claim flowing from rejection of the lease, § 502(b)(6). Franklin's claim, under the first amended plan, was therefore an unsecured lease rejection claim. SER281.

This position was hardly "frivolous." Although Franklin describes the City as "conced[ing] defeat" on the issue, OB8, the City believed—rightly, as it turned out—that Franklin's secured claim would be no more, and likely less, than any administrative rent plus the unsecured claim capped by § 502(b)(6) if Franklin's claim were treated as an unexpired lease that the City rejected. And of course, as the City stated at the time, the City wanted "to stop wasting valuable time and resources on litigating the adversary proceeding so that the parties could focus on the main event: confirmation of the Plan." SER541. The Bankruptcy Court agreed that "anything that actually simplifies the process will probably help everybody." SER538. "Streamlin[ing]" proceedings and "narrow[ing] the issues," SER532-33, 535, demonstrates *good faith*, especially in a bankruptcy case.

C. All the cases cited by Franklin are easily distinguishable.

Franklin cites to a grab bag of cases in support of its good faith argument. Not only are they easily distinguishable; if anything, they serve to illustrate the wide gap between the City's good faith efforts to forge a confirmable plan and actual bad faith.

For instance, Franklin cites *Wright v. City of Coral Gables*, 137 F.2d 192 (5th Cir. 1943), as "instructive" and seizes on that court's statement that the debtor "bludgeon[ed]" those with whom it could not make "settlements satisfactory to itself." OB78, 80. But the circumstances of the two cases could not be more dissimilar. In *Wright*, the debtor city completed a voluntary plan in 1937 and, after 94% of creditors had accepted, abandoned the plan and sought to deal with the remaining creditors through "voluntary and often quite preferential settlements." 137 F.2d at 195. The city came to settlements with all but two of its remaining creditors, and in doing so "made it plain that the consents were not requested as a part of a plan." *Id.* Nevertheless, in 1940, the city sought to revive its plan "under changed conditions for the sole purpose of forcibly scaling the debts of nonassenting creditors." *Id.* at 196. This is the "bludgeon[ing]" to which the court referred: The debtor attempted to use settlements that were reached independent of (and subsequent to) an already completed plan—and which it assured creditors were *not* being negotiated as part of any plan—to force the remaining creditors to accept plan treatment worse than that given to other claims of the same type. *Id.* at 195-96.

The process discussed in *Wright* is a relic with no modern analog, and Franklin's attempt to equate these cases is both forced and misleading. Moreover, the bad faith acts cited in *Wright* are nothing like the treatment Franklin complains of, which is the common situation where certain claims in its class are held by creditors who also have claims in another class.

The other cases cited by Franklin similarly involve clear bad faith actions, completely incomparable to the City's conduct, such as ramming through last minute changes to favor a third party, *In re Wolf Creek Valley Metro. Dist. No. IV*, 138 B.R. 610, 613-14 (D. Colo. 1992); improper payments to or favorable treatment for insiders, *In re Val-Mid Assocs., L.L.C.*, No. 4:12-BK-20519-EWH, 2013 WL 3049235, at *3-4 (Bankr. D. Ariz. June 14, 2013); *In re Multiut Corp.*, 449 B.R. 323, 342 (Bankr. N.D.

Ill. 2011); and breaches of fiduciary obligations, *Avon Park*, 311 U.S. at 144-45.

Meanwhile, two cases cited by Franklin actually undercut its position. *In re Pierce Cnty.*, 414 B.R. at 718-19 (finding bad faith where debtor prevented investigation of possible sources of creditor payments, but holding it was not necessary to apply every possible source of payment); *In re Mount Carbon*, 242 B.R. at 41 (finding bad faith where governmental entity "abandon[ed] provision of public services" in order to "unfairly favor[] a single landowner").

IV. The Bankruptcy Court Correctly Calculated the Amount of the Retiree Health Benefit Claims.

The Bankruptcy Court correctly rejected Franklin's argument that the allowed amount of the Retiree Health Benefit Claims must be reduced to present value, relying on the plain language of § 502(b) and the structure of the Bankruptcy Code. Section 502(b) requires that a court "determine the amount of [a] claim," in contrast to ten other Code provisions that require a determination of "value." *See* §§ 1129(a)(7), (9), (15); 1129(b)(2); 1173(a)(2); 1225(a)(4), (5); 1325(a)(4), (5); 1328(b)(2). The City hired Segal to calculate that amount, the Bankruptcy Court credited it, and Franklin does not challenge it here.[9] SER384; ER460-65. Section 502(b)'s requirements are satisfied.

Unable to overcome the text of § 502(b), Franklin argues that "generally accepted accounting principles" require present value discounting. OB69-71. This argument misses the point. Neither accounting practices nor the GASB standards have any bearing on what the text of § 502(b) requires. That is a question of law about which none of Franklin's witnesses was competent to testify. *See In re Downey Reg'l Med. Ctr.-Hosp., Inc.*, 441 B.R. 120, 129 (B.A.P. 9th Cir. 2010). The legal question presented is whether the Retiree Health Benefit Claims *must* be discounted where the language of the Bankruptcy Code neither allows nor requires such discounting, and where Congress could have but did not use clear language to require discounting to present value.

[9] Franklin cites generally to the report and testimony of its expert, who purported to identify errors in Segal's methodology, *see*, *e.g.*, OB70 n.145, 71 n.146, but Franklin does not challenge Segal's $545 million calculation on appeal. *See Entm't Research Grp., Inc. v. Genesis Creative Grp., Inc.*, 122 F.3d 1211, 1217 (9th Cir. 1997) ("We review only issues which are argued specifically and distinctly in a party's opening brief.").

A. The plain language of § 502(b) requires a court to determine the amount of a claim, as distinct from the value of a claim.

"It is a well-established canon of statutory interpretation that the use of different words or terms within a statute demonstrates that Congress intended to convey a different meaning for those words." *S.E.C. v. McCarthy*, 322 F.3d 650, 656 (9th Cir. 2003). A court "must presume that Congress intended a different meaning when it uses different words in connection with the same subject." *Ariz. Health Care Cost Containment Sys. v. McClellan*, 508 F.3d 1243, 1250 (9th Cir. 2007).

The Bankruptcy Code uses specific language where it requires claims or other property to be discounted to present value. In the ten provisions that require such a discounting, the Bankruptcy Code requires courts to "determine the *value*" as of a specific date. *See* §§ 1129(a)(7), (9), (15); 1129(b)(2); 1173(a)(2); 1225(a)(4), (5); 1325(a)(4), (5); 1328(b)(2) (all emphasis added). In sharp contrast, § 502(b) requires bankruptcy courts to "determine the *amount*" of a claim. (emphasis added). An "amount" is simply a "total number or quantity." *Webster's Third New Int'l Dictionary* 72 (1993 ed.). As the Third Circuit explained in *In re Oakwood Homes Corp. ("Oakwood")*, "'amount' does not mean the same thing as 'value.'" 449

F.3d 588, 597 (3d Cir. 2006). "[W]here the Bankruptcy Code intends a court to discount something to present value, the Code clearly uses the term 'value, as of' a certain date." *Id.* The *Oakwood* court reasoned that since § 502(b) does not use that term, it does not require discounting to present value. *Id.*

The Third Circuit also noted that Congress's decision in this regard is in line with the overarching principle that the Bankruptcy Code accelerates the maturity of future obligations to the petition date. *Id.* at 602 ("The general rule of both the Bankruptcy Code and § 502(b) … is acceleration to the date of filing of the bankruptcy petition … not the *lack* of acceleration." (emphasis in original)); *see* H.R. Rep. No. 95-595, at 353-54 (1977) (section 502(b) stands for the principle that "bankruptcy operates as the acceleration of the principal amount of all claims against the debtor").

Franklin claims that this plain-language reading is a "false distinction" and argues that the sections of the Bankruptcy Code calling for a determination of value "concern the value of property distributed by the debtor," as opposed to "claims asserted against the debtor." OB73-74 (emphasis omitted). This argument is unavailing because whether the Code references debtor distributions or creditor claims has no impact on the fact that the terms "amount" and "value" have distinct meanings. Moreover, Franklin's purported distinction directly contradicts the language of these sections. For instance, § 1129(b)(2)(a)(i)(II) provides:

> that each holder of a claim of such class [of secured claims] receive on account of such claim deferred cash payments totaling at least the allowed *amount* of such claim, of a *value,* as of the effective date of the plan, of at least the *value* of such holder's interest in the estate's interest in such property.

(emphasis added). Had Congress said the *value* of the claim, or if "amount" and "value" were given the same meaning, the nonconsenting creditor in a § 1129(b)(2)(a)(i)(II) analysis would suffer two discounts.

Franklin's attempt to coopt *Oakwood* is meritless. It ignores the court's careful analysis, and instead poaches quotes that appear to support its desired result while claiming, shockingly, that it "holds in Franklin's favor." OB74-75. This despite the fact that the clear holding of the case is directly to the contrary: "We conclude that the language used in § 502(b) does not clearly and unambiguously require discounting an interest-bearing obligation to present value in light of the words' plain meanings and the language used elsewhere in the Bankruptcy Code," 449 F.3d at 603.

Franklin attempts to manufacture a distinction between interest-bearing and non-interest-bearing obligations based on *Oakwood*'s discussion of a "double discount." OB74-75. While *Oakwood* does hold that discounting the principal component of a claim when unmatured interest already has been disallowed under § 502(b)(2) would be an impermissible "double discount," there is no reason why the Third Circuit's statutory interpretation and analysis should be any different where unmatured interest is not involved. Otherwise, the very meaning of the words "amount of such claim … as of the date of the filing" would take on a different meaning from case to case. That cannot be right. Section 502(b) calls for determination of the amount, and not the value, of a claim.

B. Discounting claims to present value is not among the enumerated exceptions to § 502(b).

Franklin's argument fails for another reason: Section 502(b) contains a list of expressly enumerated exceptions that limit the allowance of certain claims—*e.g.*, § 502(b)(2) (unmatured interest), (6) (future rent), and (7) (termination of employment contract). None calls for disallowing a claim to the extent it exceeds its discounted present value. Congress must be assumed to have acted intentionally in its choice of exceptions. Had it wanted to include a discounting requirement for future obligations among the § 502(b) exceptions, it would have done so explicitly. Reading in a new, general § 502(b) exception would render the other exceptions superfluous: "If § 502(b) required all claims to be present-valued, there would be no need for [the] exceptions." *In re Gretag Imaging, Inc.*, 485 B.R. 39, 46 (Bankr. D. Mass. 2013).

C. The authorities cited by Franklin are not persuasive.

The authorities Franklin claims are to the contrary (i) rely on non-bankruptcy law mandating present valuing, (ii) analyze irrelevant § 502(b) exceptions, or (iii) are no longer good law.

Each of Franklin's key cases—*In re Chateaugay Corp.*, 115 B.R. 760 (Bankr. S.D.N.Y. 1990); *In re CF&I Fabricators*, 150 F.3d 1293 (10th Cir. 1998); and *In re CSC Indus.*, 232 F.3d 505 (6th Cir. 2000)—involves ERISA claims. ERISA, unlike the Bankruptcy Code, explicitly requires discounting to present value. *In re Chateaugay Corp.*, 115 B.R. at 767; 29 U.S.C. §§ 1301(a)(17), 1362(b)(1). The cases do contain passing suggestions, without the benefit of statutory or doctrinal analysis, that the Bankruptcy Code provides for such discounting, *id.*; *In re CSC Indus.*, 232 F.3d at 508; *In re CF & I*, 150 F.3d at 1300, but this language is clearly unconsidered *dicta*. These cases are neither helpful nor persuasive because they conflate the requirements of ERISA with those of the Bankruptcy

Code without considering the actual language of § 502(b) in the Code's larger context.

The other cases cited by Franklin are similarly unavailing. Several merely parrot the broad language of the three ERISA cases, or contain no analysis whatsoever. *See In re Trace Int'l Holdings, Inc.*, 284 B.R. 32 (Bankr. S.D.N.Y. 2002); *In re Thomson McKinnon Secs., Inc.*, 149 B.R. 61, 75 (Bankr. S.D.N.Y. 1992); *Kucin v. Devan*, 251 B.R. 269 (D. Md. 2000). The district court in *In re O.P.M. Leasing Servs.*, *Inc.*, improbably found that the mere requirement in section 502(b) that a claim for rejection of an executory contract be determined as of the petition date should be interpreted to mandate a discount to present value. 79 B.R. 161, 161-67 (S.D.N.Y. 1987). The Third Circuit dismantled this reasoning: "Viewed against the remainder of the Bankruptcy Code, 'amount of such claim … as of the date of filing of the petition' simply does not clearly and unambiguously require discounting a claim to present value. Rather, 'the *full face amount* of a debt instrument is the *proper amount of claim* in a bankruptcy case' where, as here, original issue discount is not at issue." *Oakwood*, 449 F.3d at 596-97 (quoting 4 *Collier* ¶ 502.03 (Alan N. Resnick & Henry J. Sommer eds., 15th rev. ed. 2005) (emphasis *Oakwood*'s)).

Further, one of Franklin's purported authorities, *In re Loewen Grp. Int'l, Inc.*, 274 B.R. 427 (Bankr. D. Del. 2002), is no longer good law. *Oakwood*, 449 F.3d at 601 ("We reject … the *Loewen* court's baseline conclusion that § 502(b) is clear and unambiguous."). The Third Circuit's rejection of *Loewen* also implicitly guts Franklin's reference to *In re Wisconsin Engine Co.*, 234 F. 281 (7th Cir. 1916), which *Loewen* cites and which, as a case that is focused on the provability/allowability dichotomy rejected and superseded by the adoption of § 502 in 1978, has no bearing on the language or interpretation of § 502(b).

The Bankruptcy Court correctly held that § 502(b) did not require discounting. ER464-65.[10]

V. The Court Correctly Concluded that the City Satisfied § 943(b)(3)'s Fee Disclosure Requirement.

Finally, Franklin challenges the Bankruptcy Court's finding that the City satisfied § 943(b)(3). That subsection requires that "all amounts to be paid by the debtor or by any person for services or expenses in the case or

[10] The Bankruptcy Court also found that if present value discounting was required, the 4.5% discount rate proposed by Franklin was incorrect, and that a lower rate would be appropriate. ER464-65. If this Court were to find that discounting is required, a remand would be necessary for a determination of the proper rate.

incident to the plan have been fully disclosed and are reasonable." Franklin does not argue that the City failed to disclose any fees "to be paid" in the future. It argues instead that the words "to be paid" mean "*all* of the debtor's fees and expenses in a chapter 9 case regardless of whether or not previously paid." OB83 (emphasis Franklin's). Once again, Franklin ignores plain language and unmistakable statutory context.

A. The Supreme Court has "stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there." *Conn. Nat. Bank v. Germain*, 503 U.S. 249, 253-54 (1992). When "the words of a statute are unambiguous, then, this first canon is also the last: 'judicial inquiry is complete.'" *Id.* (quoting *Rubin v. United States*, 449 U.S. 424, 430 (1981)); *see also Barnhart v. Sigmon Coal Co.*, 534 U.S. 438, 461-62 (2002).

Section 943(b)(3) on its face refers to fees "to be paid," and the Bankruptcy Court properly held that these words are unambiguous as to what is required. The Court explained: "[I]n accordance with the verb tense, 'to be paid,'" it is only a "promise of extra payments … that have not been paid … or that will have to be paid in the future, that need to be disclosed." ER454. Simply put, a thing "to be" done has not been done yet.

The phrase *to be paid* means what it says: it is prospective language that means "fees that *will* be paid in the future," not retrospective language that means "fees that *have been* paid during the course of the case." As the Bankruptcy Court held, the City complied with § 943(b)(3), and even went beyond it by voluntarily providing a summary of the professional fees it incurred as a show of good faith. ER756-59.

This straightforward reading is confirmed by the broader statutory context of the Bankruptcy Code. Section 1129(a)(4) requires that "[a]ny payment *made or to be made* ... has been approved by ... the court as reasonable." (emphasis added); *see* § 329 (requiring "a statement of the compensation paid or agreed to be paid"). In § 901(a), Congress expressly enumerated those sections of the Bankruptcy Code that it saw fit to incorporate into chapter 9, including five of the chapter 11 plan confirmation requirements listed in § 1129(a). But Congress left § 1129(a)(4)'s retrospective fee disclosure requirement behind, instead drafting § 943(b)(3) to require only that "all amounts to be paid ... have been fully disclosed and are reasonable." Similarly, Congress chose not to incorporate into chapter 9 other Bankruptcy Code sections requiring retrospective approval of fees, §§ 329-30.

The reason Congress decided to treat chapter 9 cases differently from chapter 11 is just as clear: Based on the Tenth Amendment and respect for state and local sovereigns, Congress sought to minimize federal interference with the exercise of governmental authority. Accordingly, § 904 limits the power of the court to control or affect a chapter 9 debtor's "political or governmental powers," "property or revenues," or the "use or enjoyment of income-producing property." *See generally In re City of Stockton, Cal.*, 478 B.R. 8, 19-20 (Bankr. E.D. Cal. 2012) (discussing Tenth Amendment underpinnings of § 904). Those same concerns informed Congress's decision not to embrace the chapter 11 model of fee reporting, declining to impose retrospective fee review along with the additional and otherwise applicable procedures for court approval of professionals set forth in §§ 326-30.

B. Franklin's attempt to overcome this rests on the bankruptcy court's decision in the City of Detroit's chapter 9 case, in which it refused to adhere to the plain text and held that § 943(b)(3) required retrospective analysis of fees. *Detroit*, 524 B.R. at 205-08. This Court should decline Franklin's invitation to do the same. The bankruptcy court in *Detroit* admitted that "[t]he plain language of § 943(b)(3) requires only that fees 'to be paid' must be reasonable," *id.* at 208, and recognized that the Code uses different language elsewhere, but nonetheless convinced itself that Congress could not have meant what it said, *id.* at 205-08. As this Court has explained, however, "the court's role is to interpret and apply statutes, not to rewrite them." *In re Tanzi*, 297 B.R. 607, 613 n.7 (B.A.P. 9th Cir. 2003). Where, as here, a "statute's language is plain, 'the sole function of the courts is to enforce it according to its terms.'" *United States v. Ron Pair Enters., Inc.* 489 U.S. 235, 241 (1989).

Franklin, following the *Detroit* ruling's lead, cites *Avon Park*, 311 U.S. 138. The debtor in *Avon Park* proposed a plan of composition under which its fiscal agent would be compensated for its services by an assessment imposed on participating bondholders *after* confirmation. *Avon Park*, 311 U.S. at 145, 147; *Detroit*, 524 B.R. at 210. That in no way suggests that the later-enacted § 943(b)(3) requires retrospective review—retrospective review was not even at issue in *Avon Park*.

The *Detroit* court read *Avon Park* to hold that, "as a court of equity, a bankruptcy court has the authority, 'guided by equitable doctrines and principles,' to 'safeguard the public interest.'" 524 B.R. at 210 (quoting *Avon Park*, 311 U.S. at 145). The court's general equitable powers, however, are not a license to ignore the intent of Congress as expressed through the plain statutory text or to second guess Congress's considered choice. As the Supreme Court has held, "[t]he short answer to these arguments is that whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206-07 (1988).

CONCLUSION

For the foregoing reasons, this Court should affirm the Bankruptcy Court's confirmation of the Plan.

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Respectfully submitted,

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CERTIFICATION PURSUANT TO BAP RULE 8015(a)-1(b)

The undersigned certifies that the following parties have an interest in the outcome of this appeal. These representations are made to enable judges of the Panel to evaluate possible disqualification or recusal:

1. City of Stockton, California
2. Franklin High Yield Tax-Free Income Fund
3. Franklin California High Yield Municipal Fund
4. Official Committee of Retirees
5. California Public Employees' Retirement System
6. Stockton Police Officers Association
7. Stockton Police Managers Association
8. Stockton City Employees Association
9. Stockton Professional Firefighters – Local 456
10. Operating Engineers Local No. 3
11. Assured Guaranty Corp.
12. Assured Guaranty Municipal Corp.
13. National Public Finance Guarantee Corp.
14. Wells Fargo Bank, National Association, as Indenture Trustee

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CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Federal Rule of Bankruptcy Procedure 8015(a)(7)(C), as modified by this Court's order of January 12, 2015, because it contains 20,900 words, excluding the parts of the brief exempted by Federal Rule of Bankruptcy Procedure 8015(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Federal Rule of Bankruptcy Procedure 8015(a)(5) and the type style requirements of Federal Rule of Bankruptcy Procedure 8015(a)(6) because it has been prepared in a proportionally spaced typeface using Microsoft Word 14-point Century Schoolbook font.

May 28, 2015

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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing brief with the Clerk of the Court for the Bankruptcy Appellate Panel for the Ninth Circuit by using the appellate CM/ECF system on May 28, 2015, which will automatically serve all parties of record who are registered CM/ECF users. I further certify that parties of record to this appeal who are not CM/ECF users have consented in writing to electronic service, and that I have served these parties via email.

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