

7

1 WINSTON & STRAWN LLP
Lawrence A. Larose (admitted *pro hac vice*)
2 llarose@winston.com
200 Park Avenue
3 New York, NY 10166-4193
Telephone: (212) 294-6700
4 Facsimile: (212) 294-4700

5 WINSTON & STRAWN LLP
Matthew M. Walsh (SBN: 175004)
6 mwalsh@winston.com
333 S. Grand Avenue, 38th Floor
7 Los Angeles, CA 90071-1543
Telephone: (213) 615-1700
8 Facsimile: (213) 615-1750

9 Attorneys for Creditor
NATIONAL PUBLIC FINANCE
10 GUARANTEE CORPORATION

11
12 **UNITED STATES BANKRUPTCY COURT**
13 **EASTERN DISTRICT OF CALIFORNIA, SACRAMENTO DIVISION**

14 In re:
15 CITY OF STOCKTON, CALIFORNIA,
16 Debtor.

) Case No. 12-32118
) D.C. No. OHS-1
) Chapter 9

) **NATIONAL PUBLIC FINANCE**
) **GUARANTEE CORPORATION'S**
) **MOTION *IN LIMINE* #2 TO**
) **EXCLUDE ANY EVIDENCE**
) **GENERATED POSTPETITION**
) **CONCERNING THE RATIONALE**
) **FOR THE CITY OF STOCKTON,**
) **CALIFORNIA'S DECISION NOT TO**
) **NEGOTIATE WITH OR TO SEEK**
) **TO IMPAIR THE CALIFORNIA**
) **PUBLIC EMPLOYEES'**
) **RETIREMENT SYSTEM PRIOR TO**
) **THE FILING OF THIS CHAPTER 9**
) **PETITION**

) Date: March 20, 2013
) Time: 9:30 a.m.
) Dept: Courtroom 35
) Judge: Hon. Christopher M. Klein

27
28

1 National Public Finance Guarantee Corporation (“National”), a creditor and party in interest,¹
2 hereby requests that the Court enter an order excluding any evidence of postpetition actions,
3 conduct, deliberations, or documents concerning the rationale for the City of Stockton, California’s
4 (the “City”) decision not to negotiate with or to seek to impair the California Public Employees’
5 Retirement System (“CalPERS”) prior to the filing of its chapter 9 petition.² In support of this
6 Motion, National states as follows:

7 **I. INTRODUCTION**

8 1. To be eligible as a debtor in chapter 9, the City must demonstrate, among other
9 things, that (i) before filing its petition it either negotiated in good faith with its creditors but was
10 unable to reach an appropriate agreement or was unable to negotiate with its creditors because such
11 negotiations were impracticable; and (ii) it filed its bankruptcy petition in good faith. *See* 11 U.S.C.
12 §§ 109(c)(5), 921(c).

13 2. The evidence at trial will show that the City did not negotiate with or seek to impair
14 CalPERS – the City’s largest unsecured creditor by its own admission - before the bankruptcy
15 petition date. However, *after* the petition date, at the time when the Objecting Parties³ filed
16 eligibility objections criticizing the City’s failure to engage in good faith prepetition negotiations
17 with all of its creditors (including CalPERS), the City sought to remedy its prepetition failure by
18 initiating an intensive exercise with its outside consultant, Management Partners, to generate
19 evidence justifying its previously uninformed decision not to engage with or seek impairment of
20 CalPERS.

21
22 ¹ As detailed in National’s Joinder of Creditor National Public Finance Guarantee Corporation to
23 Indenture Trustee’s Limited Objection to the Debtor’s Emergency Motion for Leave to Introduce
Evidence Relating to Neutral Evaluation Process under Government Code Section 53760.3(Q) [Dkt.
No. 78], National is a secured creditor of the City and party in interest in this case.

24 ² In conjunction with this Motion, National has also filed its Motion *in Limine* #1, which seeks to
25 exclude the City from introducing any evidence concerning the rationale (whether developed pre- or
26 postpetition) for its decision not to negotiate with or to seek to impair CalPERS, on the ground that
27 the City shielded from discovery much of the evidence in this regard. This Motion serves as an
independent basis for excluding the postpetition evidence that is partially the subject of the Motion
in Limine #1.

28 ³ The Objecting Parties include National, Assured Guaranty Corp., Assured Guaranty Municipal
Corp., Wells Fargo Bank, National Association as Indenture Trustee, and Franklin High Yield Tax-
Free Income Fund and Franklin California High Yield Municipal Fund.

1 3. This Motion seeks to exclude the City from presenting evidence at the eligibility trial
2 of those belated postpetition efforts to justify its prepetition conduct – evidence that is irrelevant to
3 the good faith analysis under sections 109(c) and 921(c) of the Bankruptcy Code or any other matter
4 at issue in the upcoming trial. Accordingly, National hereby requests that the Court enter an Order
5 pursuant to Rule 402 of the Federal Rules of Evidence excluding the introduction of any and all
6 evidence of the City’s postpetition actions, conduct, deliberations, or documents concerning the
7 City’s rationale for its prepetition decision not to negotiate with or to seek to impair CalPERS as part
8 of its restructuring efforts.

9 **II. BACKGROUND**

10 4. On June 28, 2012 (the “Petition Date”), the City commenced this case by filing a
11 voluntary petition for relief under chapter 9 of the Bankruptcy Code.

12 5. On August 8, 2012, National submitted its Objection to the City of Stockton’s
13 Qualifications Under Section 109(c) [Dkt. No. 477] (the “Objection”).⁴ Among other things, the
14 Objection asserts that (a) the City did not meet its obligation under section 109(c)(5)(B) to negotiate
15 in good faith with its creditors because it failed to negotiate with CalPERS, the holder of the largest
16 unsecured claim against the City, (b) negotiations with CalPERS were not impracticable under
17 section 109(c)(5)(C), and (c) the City did not meet its obligation under section 921(c) to file its
18 Petition in good faith.

19 6. Pursuant to the Court’s Scheduling Order [Dkt. No. 558], Stipulation and Order
20 Modifying Eligibility Scheduling Order [Dkt. No. 579], and Stipulation and Order Modifying
21 Eligibility Scheduling Order [Dkt. No. 623], National conducted discovery and took depositions of
22 the City and of CalPERS.⁵

23 7. On December 14, 2012, based on this discovery, National submitted its Supplemental
24 Objection to the City of Stockton’s Qualifications Under Sections 109(c) and 921(c) [Dkt. No. 635]
25 (the “Supplemental Objection”).

26 _____
27 ⁴ Capitalized terms not otherwise defined herein shall have the meaning ascribed to such terms in the
Objection.

28 ⁵ Excerpts of the deposition testimony referenced herein are attached as Exhibits A-E to the
Declaration of Matthew M. Walsh in Support of National’s Motion (“Walsh Decl.”) filed herewith.

1 8. On February 15, 2013, the City submitted its Reply to Objections to its Statement of
2 Qualifications Under Section 109(c) of the United States Bankruptcy Code [Dkt. No. 707] (the
3 “Reply”).

4 9. A trial on the City’s eligibility to be a debtor under chapter 9 of the Bankruptcy Code
5 is set to begin on March 25, 2013.

6 **III. DISCUSSION**

7 10. This Court held recently that “[t]he burden of proof, at least as to the five § 109(c)
8 elements, is on[] the municipality as the proponent of voluntary relief.” *In re City of Stockton*, 475
9 B.R. 720, 725 (Bankr. E.D. Cal. 2012) [*Stockton I*]; *see also Int’l Ass’n of Firefighters, Local 1186*
10 *v. City of Vallejo (In re City of Vallejo)*, 408 B.R. 280, 289 (9th Cir. BAP 2009). As relevant here,
11 the City must prove that, *before* filing its chapter 9 petition, either it negotiated in good faith with its
12 creditors but was unable to reach appropriate agreement, or that it was unable to negotiate with its
13 creditors because such negotiations were impracticable. 11 U.S.C. § 109(c)(5).

14 11. As a matter of common sense, the question whether the City negotiated in good faith
15 under section 109(c) focuses only on events that occurred *prior to* the Petition Date. Indeed, the
16 City concedes that whether the City negotiated in good faith before the Petition Date should also be
17 adjudged by the City’s prepetition actions. *See, e.g., City’s Eligibility Memorandum* at 38 (“Section
18 109(c)(5) provides four alternative tests for proving that the City attempted to negotiate with its
19 creditors *before* filing its petition.”) (emphasis added).

20 12. Similarly, section 921(c) of the Bankruptcy Code requires the City to prove that it
21 “file[d] the petition in good faith.” 11 U.S.C. § 921(c). The plain language of this provision
22 indicates that it concerns the City’s good faith as of the Petition Date – something that logically can
23 be assessed only in consideration of what the City knew as of the Petition Date without reference to
24 information or materials generated thereafter.

25 13. During discovery, however, the City admitted time and time again that prior to the
26 Petition Date it had done little or no factual study or analysis in support of its decision not to
27 negotiate with or to seek to impair CalPERS. *See Haase Dep. 88:15-19* (unable to recall any study
28 or analysis conducted by the City or any outside consultant, aside from materials prepared after the

1 AB 506 process, concerning the City’s decision not to impair CalPERS); *see also* Montes Dep.
2 115:4-10 (unable to recall any study or analysis concerning the potential impact of not offering a
3 CalPERS plan); Goodrich Dep. 194:15-18 (the City did not calculate the “potential savings from a
4 restructuring of the pension benefit obligation”). Nor did the City consider alternatives to CalPERS,
5 such as forming an independent benefit plan or joining an existing defined benefit plan. *See* Deis
6 Dep. 206:15-21; *see also* Haase Dep. 89:8-13 (unaware of any “effort to study alternative benefit
7 structures” to replace CalPERS).

8 14. It was only *after* the filing of its chapter 9 petition (and upon learning that creditors
9 would object on this ground) that the City tried to construct an after-the-fact justification for its
10 prepetition decision not to negotiate with or to seek to impair CalPERS. In particular, National filed
11 its Objection on August 8, 2012. On that very same day (nearly a month and a half after the Petition
12 Date), City representatives met with the City’s outside consultant, Management Partners, to begin
13 developing a “business case” to support its decision not to impair CalPERS. *See* Haase Dep. 82:20-
14 83:14; Goodrich Dep. 267:15-268:2. Teresia Haase testified that “[t]his was the first meeting [she]
15 recall[s] where the purpose . . . was to discuss the information we may want to gather to help us
16 understand what the market was with respect to PERS or a PERS reciprocal defined retirement
17 benefit system.” Haase Dep. 84:4-12. The objective of these meetings was “to make the business
18 case for remaining current and in good standing with CalPERS” for purposes of providing “evidence
19 in [the City’s] eligibility case.” *See* Walsh Decl., Exh. F (Management Partners’ Follow-Up Notes
20 from August 8, 2012 Meeting with Ann Goodrich and Teresia Haase as well as SDT Meeting); *see*
21 *also* Goodrich Dep. 280:12-20 (testifying that the purpose of seeking this information was because
22 “we anecdotally knew most of this information[,] . . . [b]ut we wanted to be able to specifically state
23 that we had checked with all these jurisdictions and that - that it wasn’t just based on anecdotal
24 understanding of what common practices are.”). A month later, Management Partners was
25 continuing to work up its “CalPERS Business Case Outline.” *See* Walsh Decl., Exh. G (Email from
26 Andy Belknap to Teresia Haase and Ann Goodrich, dated September 10, 2012, discussing an
27 updated version of the CalPERS Business Case Outline).

28

1 15. At about this same time, City Manager Bob Deis met with Eric Jones, Stockton's
2 Chief of Police, and requested that Jones write a memorandum describing what Jones postulated
3 could be the impact should the City reduce its pension benefits. Jones Dep. 256:7-258:13 (testifying
4 that Deis asked Jones approximately one to two weeks before August 14, 2012 to write a
5 memorandum discussing the consequences of "an assertion being made that possibly the PERS
6 contract would be broken"). Jones responded with an August 14, 2012 memorandum speculating
7 that, in his view, the City would face a "mass exodus" from its police force should pension benefits
8 be reduced. Walsh Decl. Exh. H at 4 (Memorandum to Governor Jerry Brown and other California
9 state officials from City Manager Deis calling for state reform of pension laws, dated August 15,
10 2012). This assertion of a "mass exodus" – borne out of the City's postpetition efforts to justify its
11 prepetition CalPERS decision – has resulted in significant discovery and debate in the eligibility
12 proceedings between the City and the Objecting Parties.

13 16. The next day, August 15, 2012, City Manager Deis sent a memorandum to Governor
14 Jerry Brown and other California state officials calling for state reform of pension laws. *See* Walsh
15 Decl., Exh. H at 1-3. In this memorandum, Deis contends that, without state-level reform, "cities
16 like Stockton will then find themselves at a massive competitive disadvantage in recruiting and
17 retaining employees. This is particularly true in the case of police officers, . . . who almost certainly
18 will leave in increasing numbers if Stockton is forced to reduce its pension obligations while other
19 cities do not or cannot make similar adjustments." *Id.* at 1. Notably, Deis makes no secret that his
20 call for reform coincides with the objections to the City's chapter 9 petition. *Id.* at 2 ("Substantial
21 objections to our bankruptcy filing have been filed against the City because we have not unilaterally
22 reduced our pension payments to CalPERS or negotiated such reductions with CalPERS.").

23 17. Because all of these efforts (as well as others) by the City to justify its prepetition
24 decision not to negotiate with or seek to impair CalPERS occurred *only after* the Petition Date in a
25 transparent effort to shore up the City's deficient prepetition decision-making process, they are
26 irrelevant to the good faith analysis under sections 109(c) and 921(c), and all such evidence should
27 be precluded at trial. *See* Fed. R. Evid. 402 ("Irrelevant evidence is not admissible.").
28

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

WHEREFORE, National respectfully requests that this Court issue an order excluding at trial any evidence of postpetition actions, conduct, deliberations, or documents concerning the rationale supporting the City’s prepetition decision not to negotiate with or to seek to impair CalPERS.

Dated: March 13, 2013

WINSTON & STRAWN LLP

By: /s/ Lawrence A. Larose
Lawrence A. Larose (admitted *pro*
hac vice)

and

/s/ Matthew M. Walsh
Matthew M. Walsh

Attorneys for Creditor
National Public Finance
Guarantee Corporation