The Official Committee of Retirees (the “Committee”) submits this memorandum to express its support for confirmation of the City of Stockton’s First Amended Plan of Adjustment (November 15, 2013) (the “Plan”).

I. The Retiree Settlement

The Committee participated in extensive mediation negotiations with the City that resulted in the Retiree Settlement provided in the Plan. (Plan, Definition 156.) The Retiree Settlement provides that the Committee would support confirmation of the Plan consistent with the settlement, including (i) the treatment provided for the Retiree Health Benefit Claims in Class 12 of the Plan, ($5.1 million to be distributed pro-rata among approximately 1,100 Retiree Health...
Benefit Claims totaling approximately $545,000,000, resulting in a percentage distribution of approximately 0.935% of each Retiree Health Benefit Claim)¹ and (ii) the unimpairment of retirees pension benefits as CalPERS Pension Plan Participants as provided in Class 15 of the Plan.

The Committee supports confirmation of the Plan even though the Retiree Health Benefit Claimants stand to lose hundreds of millions of dollars in health benefit coverage that was earned and promised to them over many years of dedicated service and the retirees will receive less than the cost of premiums for one year for replacement health insurance coverage for most retirees on account of their Retiree Health Benefit Claims. (See www.coveredca.com/shopandcompare.) The retirees will retain their rights to their pensions as unimpaired under the Plan, as there are substantial justifications for doing so. For example, even assuming that pension rights could be modified, a substantial amount of the City’s pension obligations to retirees on account of their pension rights have already been funded and, unlike the City’s self-funded health benefits, the City’s pensions obligations involve substantial rights and obligations with a third party, CalPERS. Thus, the retirees’ retention of their pensions should not obscure the real and substantial magnitude of the retirees’ losses from confirmation of the Plan. That being said, the Committee supports confirmation of the Plan due to the reality of the City’s financial circumstances, notwithstanding the substantial sacrifices and losses of retirees that will result from the Plan as a necessary solution to the City’s financial troubles. And the City’s retirees agree. The Retirees have voted overwhelmingly to accept the plan. (Decl. of Catherine Nownes-Whitaker Regarding Tabulation and Certification of Ballots, Dkt. No. 1268.)

II. The Retiree Health Benefit Claims Should Not Be Discounted to Present Value.

Franklin Fund wrongly asserts that the Retiree Health Benefit Claims must be discounted to present value. (Franklin’s Summary Objection, III(E)(1).)

¹ See Class 12 Treatment at Section IV(M)(2) of the Plan, Unsecured Claim Payout Percentage at Definition 185 of the Plan, and the City’s Amended List of Creditors and Claims Pursuant to 11 U.S.C. §§ 924 and 925 (Retiree Health Benefit Claims) (Dkt. 1150).
First, the City’s Amended List of Creditors and Claims Pursuant to 11 U.S.C. §§ 924 and 925 (Retiree Health Benefit Claims) (Dkt. 1150) schedules the Retiree Health Benefit Claims as undisputed. Pursuant to Bankruptcy Code Sections 501, 502(a), 924 and 925, these Retiree Health Benefit Claims are deemed allowed in the scheduled amount unless objections to the claims are filed. While the Committee, the City, and Franklin Fund continue to discuss the potential for Franklin Fund’s objection to confirmation to proceed without the filing of 1,100 individual claim objections, no stipulation has yet been reached.

Second, Bankruptcy Code Section 502(b) provides for allowance of objected claims after notice and hearing in “the amount of such claim in lawful currency of the United States as of the filing date of the petition”, subject to certain exceptions set forth in Section 502(b)(1) through (9). As explained in In re Oakwood Homes Corp., 449 F.3d 588, 597 (3d Cir. 2006), “amount” means the accelerated amount of the claim as of the petition date without discounting to present value. In In re Oakwood Homes, the Court of Appeals upheld the objections of an indenture trustee for a group of bondholders to the discounting of the bondholders’ claims to present value and held that the bondholders’ claims should be allowed in the full accelerated amount of their claims.

Of course, as explained in In re Oakwood, the Bankruptcy Code does provide for discounting to present value in certain circumstances. For example, when determining the “value” of claims or payments, as opposed to the “allowance” of claims, the Bankruptcy Code calls for a present value determination. Id., See e.g. 11 U.S.C. §§ 1129(a)(7), (9), and (15); 1129(b)(2); 1173(a)(2); 1225(a)(4) and (5); 1325(a)(4) and (5); 1328(b)(2). The application of present value to determine “value” has long been established in the application of these sections.

For example, when an undersecured creditor makes an 1111(b) election, the total payments required on account of the creditor’s “allowed” claim must have a “value” of at least the present value of the creditor’s interest in the collateral. See In re Weinstein, 227 B.R. 284, 294 (B.A.P. 9th Cir. 1998). And the expressly provided exceptions in Section 502(b)(1) through (9) also include instances where the general rule of acceleration of the amount owed is not applied. Another instance where the Bankruptcy Code provides an exception to the general standard for acceleration of debt when allowing claims lies in the express exceptions set forth in Section 502.
For example, Section 502(b)(6) calculates a claim for damages resulting from termination of a real property lease “without acceleration”, and 502(b)(7) provides for calculation of certain claims arising from termination of an employment contract “without acceleration.” Thus, the Bankruptcy Code provides for present valuation where that discount is required (i.e. in the Sections providing for determination of “value” and the exceptions within Section 502) but no such provision is made for general allowance of claims, including the Retiree Health Benefit Claims. If Retiree Health Benefit Claims must be discounted to present value, then all claims must be discounted to present value, which would render meaningless the Bankruptcy Code’s express provisions regarding the value of a claim and the exceptions included within Section 502(b). It would also result in a double discounting of claims since claims would be discounted to present value for allowance and then discounted to present value again when the code sections requiring valuation are applied. Accordingly, Franklin Fund’s suggestion that Retiree Health Benefit Claims must be discounted to present value improperly expands the exceptions of Section 502(b), ignores the Code’s distinction between allowance and valuation and improperly deflates the value of Retiree Health Benefit Claims.

The Committee acknowledges that *In re Oakwood*, involved an interest-bearing claim, which one could attempt to distinguish from the Retiree Health Benefit Claims. But there is no reason to treat the Retiree Health Benefit Claims differently. As recently explained by the Bankruptcy Court in *In re Gretag Imaging*, 485 B.R. 39, 46 (Bankr. D. Mass. 2013), allowance of non-interest bearing claims should not be made by a different set of rules and the reasons for allowing interest-bearing claims as provided in *In re Oakwood* applies equally to interest-bearing and non-interest-bearing claims. Moreover, to categorize the Retiree Health Benefit Claims as non-interest bearing claims would be a mistake since retirees would be entitled to interest on a judgment for damages for the loss of retiree health benefits outside of bankruptcy. Allowing Retiree Health Benefit Claims differently depending upon whether a prepetition judgment was obtained would be improper and superimpose different standards for allowing claims depending on the status of enforcement that is not provided in the Bankruptcy Code.

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The Committee urges the Court not to follow the cases cited by Franklin Fund. Those cases wrongly misapply Bankruptcy Code sections governing classification of claims in the claims allowance analysis (e.g. Dugan v. Pension Ben Guar. Corp. (In re Rhodes, Inc.), 382 B.R. 550, 556 (Bankr. N.D. Ga. 2008) misapplying section 1123(a)(4)) or that improperly expand the exceptions of Section 502(b) to swallow the rule (e.g. Thompson v. Credit Union Fin. Group, 453 B.R. 823 (W.D. Mich. 2011); Pereira v. Nelson (In re Trace Int’l Holdings, Inc.), 284 B.R. 32 (Bankr. S.D.N.Y. 2002) which involved rejected employment contracts), or are inconsistent with the requirements of the Bankruptcy Code as explained above.

Accordingly, the Committee submits that the amounts of the Retiree Health Benefit Claims as set forth in the City’s Amended List of Creditors and Claims should not be discounted to present value and should not be a basis for denying confirmation of the Plan.

III. Conclusion

The Committee supports confirmation of the Plan as in the best interest of the City and its creditors.

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