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UNITED STATES BANKRUPTCY COURT

EASTERN DISTRICT OF CALIFORNIA

SACRAMENTO DIVISION

In re:	Case No. 2012-32118
CITY OF STOCKTON, CALIFORNIA,	D.C. No. OHS-15
Debtor.	Chapter 9
	CITY'S RESPONSE TO SUPPLEMENTAL OBJECTION OF MICHAEL C. COBB TO FIRST AMENDED PLAN
	Date: May 1, 2014 Time: 1:30 a.m. Dept: C Judge: Hon. Christopher M. Klein

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I. ARGUMENT

In the City's initial response to Michael C. Cobb's objection to the confirmation of the City's plan of adjustment,[1] the City explained that today Cobb possesses an unsecured claim for the payment of money and that it does not offend the Fifth Amendment for a bankruptcy court's confirmation order to adjust such a claim in a bankruptcy case. Further, the City's response demonstrated that treating Cobb's claim as unsecured under generally applicable bankruptcy law constitutes "just compensation" under the circumstances.

Cobb's Supplemental Objection to the Confirmation of the First Amended Plan does not meaningfully confront any of this. Instead, Cobb cobbles together a series of red herrings and platitudes, while expressing umbrage that the City even takes issue with his *$4.2 million* claim based on an easement over a strip of then-undeveloped land on which the City built a road 14 years ago. He then suggests that this Court must dismiss the entire chapter 9 case because of his objection.

Cobb's objection continues to hinge on the fundamentally unsound premise that he comes to this case as a property owner whose property rights would be compromised by the City's plan of adjustment. He does not. Indeed, he does not even come as an ordinary condemnee. He waived any right to challenge the condemnation under state law, and retains only a bare, unsecured right to challenge the amount of payment. The issue presented here is not about treating landowners as less than secured creditors. It is about treating unsecured creditors as unsecured creditors. This Court should reject Cobb's objection and confirm the plan.

A. The Plan Proposes to Adjust Only Cobb's Unsecured Right to Monetary Compensation.

For purposes of Takings Clause analysis, relevant legal interests "are created and their dimensions are defined by existing rules or understandings that stem from independent sources such as state law." *Ruckelshaus v. Monsanto*, 467 U.S. 986, 1001 (1984). California state law is clear on the dimensions of the interest Cobb asserts in this chapter 9 case: Under state law, he has

[1] We refer to the City's Response to Objection of Michael C. Cobb, Dkt. No. 1298, as "the City's initial response" and cite to it as "City's Response." We cite to the Supplemental Objection to Plan of Creditor Michael A. Cobb and Reply to City's Response, Dkt. No. 1396, as "Cobb Supp."

a bare, unsecured claim to monetary payment.

As detailed in the City's initial response, when the City condemned the strip of land on Cobb's property, it appraised the land's value and deposited $90,200 as "probable compensation," pursuant to California state law. Cal. Civ. Proc. Code § 1255.010. In 2000, Cobb withdrew the $90,200. *Cobb v. City of Stockton*, 192 Cal. App. 4th 65, 67 (Ct. App. 2011). Doing so had important legal consequences. California Civil Procedure Code Section 1255.260 explains the consequences of this withdrawal:

> If any portion of the money deposited pursuant to this chapter is withdrawn, the receipt of any such money shall constitute a waiver by operation of law of all claims and defenses in favor of the persons receiving such payment except a claim for greater compensation.

The statute is unequivocal. Once the condemnee withdraws probable compensation, the only thing left of his "claims and defenses" against the condemnor is "a claim for greater compensation." *Id.* This happens immediately, by operation of law, without qualification, reservation, exception, or need for a court order.

Cobb seeks to avoid this conclusion by suggesting that the later dismissal of the City's eminent domain proceeding somehow *unwaived* Cobb's claims. Cobb Supp. at 4. He argues that because the eminent domain proceeding was not dismissed on the merits, it is "not res judicata on any issue in that case." *Id.* Res judicata has nothing to do with it. Section 1255.260 makes absolutely clear that the act of withdrawal, "by operation of law," carries final and binding consequences in the form of a waiver of any claim but one to greater compensation. Put simply, Cobb took the $90,200 of probable compensation and has retained it ever since. He cannot put the cat back in the bag. And nowhere does the statute suggest that the strings that attached to his withdrawal by operation of statutory law somehow vanish because an eminent domain proceeding does not end in judgment on the merits.[2]

Cobb's legal claims are confined to an interest in monetary payment for an additional reason as well. As the City explained in its initial response, "where a property owner permits the

[2] Once Cobb withdrew the funds and relinquished his right to challenge the easement, there was no need for the City to seek further relief from the court. At that point, Cobb had the option of contesting the amount paid, but he chose not to do so in that forum.

completion by a public agency of the work which results in the taking of private property for a public use …. [h]is only remedy under such circumstances is proceeding in inverse condemnation to recover damages." *Frustuck v. City of Fairfax*, 212 Cal. App. 2d 345, 371 (Ct. App. 1963). This is called the doctrine of intervening public use, and it is the reason Cobb's quiet title and ejectment claims failed in his state court action. Cobb has not even attempted to refute this argument in his supplemental objection, effectively conceding that the public use doctrine operates to strip his claim down to an unsecured interest in seeking an additional monetary payment.

Cobb emphasizes that he retains legal title to the strip of land on which the City built the road. Cobb Supp. at 3-4. True, but irrelevant. Cobb retains title and the City has a permanent easement, which Cobb relinquished the right to challenge when he withdrew the deposited funds. In this bankruptcy proceeding, the City is not seeking to disturb that status quo. The City's plan of adjustment does not purport to alter legal title in anything owned by Cobb. It simply proposes to adjust the only claim Cobb advanced in this chapter 9 case: an unsecured claim to monetary payment under state law.

B. Cobb Fails to Recognize that the Takings Clause Poses No Obstacle to Adjustment of Unsecured Claims for the Payment of Money in the Bankruptcy Context.

Cobb continues to argue that the Takings Clause bars this Court from treating his interest in obtaining an additional payment from the City as an unsecured claim. The adjustment of such claims for money (whether contract, tort, or constitutional claims) that are not secured by specific property is, however, the very essence of bankruptcy law. The Takings Clause does not nullify Congress's power to prescribe laws with that effect. *See Hanover Nat'l Bank v. Moyses*, 186 U.S. 181, 188 (1902) (recognizing that Congress's bankruptcy power "includes the power to discharge the debtor from his contracts and legal liabilities").

The cases Cobb cites only confirm this. Somewhat puzzlingly, Cobb again looks to *In re Lahman Mfg. Co.*, 33 B.R. 681 (Bankr. D.S.D. 1983), for support, characterizing it as "holding that a physical taking of property is not an impairment of a 'mere contractual right' that may be adjusted under the bankruptcy laws." Cobb Supp. 7. To begin with, that is not the holding of *In*

re Lahman. Rather, *In re Lahman* holds that the Takings Clause poses no obstacle to the bankruptcy law's adjustment of a bank's unsecured claim for payment related to, but not secured by, real property. *Id.* at 686-87. What Cobb appears to take from *In re Lahman* is the uncontroversial premise, established in *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935), and its progeny, that the Takings Clause would stand as an obstacle to extinguishing a claim secured by property. But the bankruptcy law, by operating to confirm the City's plan of adjustment, would not implicate a secured claim or otherwise work any physical taking of property. Thus, cases like *In re Lahman* or *Radford* provide Cobb with no help.

At bottom, the flaw in Cobb's Takings theory is a misunderstanding of the nature of his own claim under state law and the manner in which the bankruptcy law purports to operate upon it. By confirming the City's plan of adjustment, this Court will not be effecting a physical taking of property, denying Cobb a right to real property, or adjusting a right secured by specific property. The City did act to condemn an easement over specific property over 15 years ago. The right to that easement was resolved with finality and by operation of law when Cobb withdrew the funds. Now, all that remains is an unsecured claim against the City for additional payment. That claim is properly treated like all other unsecured claims in this chapter 9 case.

The Contract Clause cases dismissed by Cobb as irrelevant make clear that when a bankruptcy court grants a municipality debt relief under a federal, generally applicable economic regulation, it is not the municipality or state that is the relevant actor, but the federal government that is acting to adjust the relevant claims under federal law. City's Response at 10-11. And because the Takings Clause does not disable the federal government from adjusting unsecured claims like Cobb's, his objections to the plan are without merit.

C. Cobb Fails to Confront Authority Demonstrating that Just Compensation in the Municipal Bankruptcy Context Must Only Be Reasonable Under the Circumstances.

In its initial response, the City cited the *New Haven Inclusion Cases*, 399 U.S. 392 (1970). City's Response at 11-13. The *New Haven Inclusion Cases* stand for the proposition that in the narrow circumstance when an entity that owes duties to the public goes through bankruptcy, the principle of "just compensation" requires consideration of the interests of all creditors, as well as

the interests of the debtor institution and the public. Cobb did not so much as cite the *New Haven Inclusion Cases*, let alone confront that opinion's teaching. Instead, he cites generalized case law standing for the proposition that "just compensation" is ordinarily market value. Cobb Supp. 5-7. This is true, as the City readily acknowledged in its initial response, but so broad as to be totally unhelpful in this context.

The *New Haven Inclusion Cases* continue to demonstrate that the concept of "just compensation" is flexible enough to accommodate a host of interests in the context of the reorganization of a public-facing entity. As the City has explained, by treating Cobb's unsecured claim neutrally under generally applicable federal bankruptcy law, the plan will pay Cobb "just compensation" under the circumstances.

D. Dismissal of the Entire Bankruptcy Case Is Inappropriate.

Cobb suggests that if this Court agrees with his position, it must dismiss the entire bankruptcy case. Cobb Supp. at 11. That is absurd. "The debtor may modify the plan at any time before confirmation …." 11 U.S.C. § 942. This Court, moreover, has the discretion to permit the City to amend its plan of adjustment if it finds the current one not confirmable. The City believes that Cobb's claim belongs in Class 12; Cobb believes otherwise. If Cobb is determined to be correct, the City should be allowed an opportunity amend the plan of adjustment to reclassify Cobb's claim, and the parties could then proceed to litigate the issue of the amount of Cobb's claim in bankruptcy court.[3] *See* 11 U.S.C. § 502(c).

[3] In its initial response, the City cited case law establishing that "[a]ttorney's fees and expenses are not embraced within just compensation for land taken by eminent domain." *Dohany v. Rogers*, 281 U.S. 362, 368 (1930). City's Response at 9 n.3. Cobb has not challenged the City's contention that his claim for attorney's fees and costs from his state court action are totally without constitutional dimension. In all events, this Court should therefore deny Cobb's objection with respect to these components of his claim.

II. CONCLUSION

For the reasons stated above and in the City's initial response, Cobb's objection should be rejected and the plan of adjustment should be confirmed.

Dated: April 25, 2014

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