

43

~~43~~

FILED

AUG - 6 2012

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF CALIFORNIA

FOR PUBLICATION

UNITED STATES BANKRUPTCY COURT  
EASTERN DISTRICT OF CALIFORNIA

In re:

CITY OF STOCKTON, CALIFORNIA,

Debtor.

Case No. 12-32118-C-9

Adversary No. 12-2302

OPINION

ASSOCIATION OF RETIRED  
EMPLOYEES OF THE CITY OF  
STOCKTON, a Nonprofit  
California Corporation,  
SHELLEY GREEN, PATRICIA  
HERNANDEZ, REED HOGAN, GLENN  
E. MATTHEWS, PATRICK L.  
SAMSELL, ALFRED J. SIEBEL,  
BRENDA JO TUBBS, TERI  
WILLIAMS, on Behalf of  
Themselves and Others  
Similarly Situated,

Plaintiffs,

v.

CITY OF STOCKTON, CALIFORNIA,

Defendant.

Before: Christopher M. Klein  
United States Bankruptcy Judge

G. Scott Emblidge (argued), Rachel J. Sater, Kathryn J. Zoglin,  
Moscone Emblidge & Sater LLP, San Francisco, California,  
for Plaintiffs.

Marc A. Levinson (argued), Norman C. Hile, John W. Killeen,  
Orrick, Herrington & Sutcliffe LLP, Sacramento, California,  
for Defendant.

1 KLEIN, Bankruptcy Judge:

2       The retired employees of the City of Stockton want this  
3 court to order the City to keep paying for their health benefits  
4 during this chapter 9 case. The difficulty is that 11 U.S.C.  
5 § 904 forbids the court from using any of its powers to  
6 "interfere with" property or revenues of a chapter 9 debtor.  
7 Accordingly, although the City's unilateral interim reduction of  
8 retiree health benefit payments may lead to tragic hardships for  
9 individuals in the interval before their claims are redressed in  
10 a chapter 9 plan of adjustment, the motion for injunctive relief  
11 must be DENIED. No relief being available and determining that  
12 this is an "arising in" core proceeding under 28 U.S.C. § 1334(b)  
13 and § 157(b)(2), the adversary proceeding will be DISMISSED.

14

15

Procedural Posture

16       This adversary proceeding was filed as a class action by the  
17 Association of Retired Employees of the City of Stockton  
18 ("ARECOS") and eight retirees on July 10, 2012, together with an  
19 Application for Temporary Restraining Order ("TRO") or  
20 Preliminary Injunction or in the Alternative Relief From Stay.

21       The retirees contend they have vested contractual rights  
22 that are protected from impairment by the Contracts Clause of the  
23 United States Constitution, a similar clause in the California  
24 Constitution, and by other provisions of California law.

25       The complaint, the application for injunctive relief, and  
26 the supporting papers conspicuously omit reference to § 904,

27

28

1 which operates as an anti-injunction statute and bars the court,  
2 without the municipality's consent, from interfering with its  
3 political or governmental powers, property or revenues, and use  
4 or enjoyment of income-producing property.

5 The court set the TRO/preliminary injunction hearing for  
6 July 23, 2012, and ordered the parties to brief the question of  
7 the effect of § 904 on this adversary proceeding. It further  
8 ordered the City to state whether, as permitted by § 904, it  
9 consents to this court resolving the interim health benefit  
10 payment dispute. Notice was also given that the court might  
11 dismiss the adversary proceeding on its own motion if it  
12 concludes that § 904 prevents all of the relief being sought.

13 At the July 23 hearing, the parties addressed all facets of  
14 the adversary proceeding, questions of jurisdiction, and judicial  
15 authority. The City did not consent to permit this court to  
16 resolve the interim health benefit payment dispute. This  
17 decision announces and explains the court's ruling.

#### 18 19 Facts

20 The City of Stockton filed this chapter 9 case on June 28,  
21 2012. The questions of the City's eligibility for chapter 9  
22 relief and whether to order relief are the subject of a separate  
23 process progressing under a schedule fixed by the court.

24 The Stockton City Council adopted a budget for the Fiscal  
25 Year commencing July 1, 2012, that, by state law, must be  
26 balanced. The required balance was achieved by cutting costs,  
27

1 including unilaterally reducing retiree health benefits.

2 This adversary proceeding seeks: an injunction prohibiting  
3 the City from implementing the retiree health benefit reduction;  
4 a declaration that the changes are unlawful; and an order  
5 compelling the City to pay for the retiree health benefit for all  
6 retirees entitled to it as of July 1, 2012; and attorney fees.<sup>1</sup>

7 For purposes of the present analysis (but without deciding  
8 the question), the retiree health benefits are regarded as  
9 bargained-for and vested contractual rights.

10 Persons whose benefits have been reduced may file proofs of  
11 claim that must be addressed in a plan of adjustment under the  
12 standards prescribed in the Bankruptcy Code for confirming plans.

13  
14 Discussion

15 Since the complaint relies on the supposed inability of the

16  
17 <sup>1</sup>The prayer in the complaint seeks:

18 1. A temporary, preliminary and permanent injunction  
19 prohibiting the City from implementing the changes to the  
Retiree Health Benefit;

20 2. A declaration under 28 U.S.C. § 2201 (The Declaratory  
21 Relief Act) that the City Retirees have a vested property  
interest in the Retiree Health Benefit and that the City's  
proposed changes eliminating the Retiree Health Benefit are  
unlawful;

22 3. An order compelling the City to maintain the Retiree  
23 Health Benefit with respect to the ARECOS' members and Class  
Plaintiffs and all other City of Stockton retirees entitled  
24 to the Retiree Health Benefit as of July 1, 2012.

25 4. For an award of reasonable attorney's fees and costs  
26 under California Civil Code §§ 1021.5 and 1033.5; California  
Government Code §§ 800 and 31536; 42 U.S.C. § 1988, and any  
other statute or rule of law authorizing such an award; and

27 Complaint, Prayer for Relief (catchall omitted).

1 City to impair contracts, we begin with basic points of  
2 constitutional law and history that give context to the § 904  
3 limitation on the court's authority. Then the focus shifts to  
4 how the plaintiffs' due process rights are protected, and thence  
5 to the jurisdictional and procedural status of this proceeding.

6  
7 I

8 This adversary proceeding is premised at bottom on the  
9 Contracts Clause of the United States Constitution: "No State  
10 shall ... pass any ... Law impairing the Obligation of  
11 Contracts." U.S. CONST., art. I, § 10, cl. 1.

12 Counsel clarified in open court that an immutable Contracts  
13 Clause is the centerpiece of plaintiffs' case. The first cause  
14 of action is: "Impairment of Contract - U.S. Constitution" and  
15 alleges that in "unilaterally changing the terms of the Retiree  
16 Health Benefit, the City impaired contractual obligations, in  
17 violation of Article I section [10] of the United States  
18 Constitution and 42 U.S.C. § 1983." Complaint, ¶ 56. The other  
19 causes of action flow from that premise.<sup>2</sup> The premise is flawed.

20  
21 <sup>2</sup>The second paragraph of the complaint states the theory:

22 2. This action seeks a temporary restraining order and  
23 declaratory and injunctive relief to stop the City from  
24 cutting health insurance premium payments for its retired  
25 employees. Termination of these health benefits is unlawful  
26 because the benefits are a form of deferred compensation  
27 which the City's retirees have already earned; therefore,  
the retirees have a vested right to these benefits protected  
by the contract clauses of the United States and California  
Constitutions. Moreover, if the City is permitted to  
terminate retiree health benefits as planned, it will

1 While the Contracts Clause is a key navigational star in the  
2 firmament of our Constitution and economic universe, it is  
3 subject to being eclipsed by the Bankruptcy Clause: "The  
4 Congress shall have Power to ... establish ... uniform Laws on  
5 the subject of Bankruptcies throughout the United States." U.S.  
6 CONST., art. I, § 8, cl. 4.

7 Significantly, the Contracts Clause bans a state from making  
8 a law impairing the obligation of contract; it does not ban  
9 Congress from making a law impairing the obligation of contract.  
10 This asymmetry is no accident.

11 The Bankruptcy Clause necessarily authorizes Congress to  
12 make laws that would impair contracts. It long has been  
13 understood that bankruptcy law entails impairment of contracts.  
14 Sturges v. Crowninshield, 17 U.S. (4 Wheat.) 122, 191 (1819).

15 In Sturges, the Supreme Court reasoned that Congress "is  
16 expressly vested with the power of passing bankrupt laws, and is  
17 not prohibited from passing laws impairing the obligation of  
18 contracts, and may, consequently, pass a bankrupt law which does  
19 impair it; whilst the states have not reserved the power of  
20 bankrupt laws, and are expressly prohibited from passing laws  
21 impairing the obligation of contracts." Id.

22 In 1936, the Supreme Court noted that the "especial purpose  
23

---

24 immediately endanger the lives of scores of elderly and ill  
25 retirees and their dependents who are financially unable to  
26 purchase health insurance. This Court's intervention is  
desperately needed to forestall preventable, imminent harm.

27 Complaint, ¶ 2.

1 of all bankruptcy legislation is to interfere with the relations  
2 between the parties concerned - to change, modify, or impair the  
3 obligation of their contracts." Ashton v. Cameron Cnty. Water  
4 Improvement Dist. No. 1, 298 U.S. 513, 530 (1936).

5 Again, in its 1938 decision validating the second municipal  
6 insolvency statute, the Court explained that the "natural and  
7 reasonable remedy through composition" is not available under  
8 state law "by reason of the restriction imposed by the Federal  
9 Constitution upon the impairment of contracts by state  
10 legislation" but the "bankruptcy power is competent to give  
11 relief." Hence, a state, by authorizing a municipality to file a  
12 case, legitimately "invites the intervention of the bankruptcy  
13 power to save its agency which the State itself is powerless to  
14 rescue." United States v. Bekins, 304 U.S. 27, 54 (1938).

15 In other words, while a state cannot make a law impairing  
16 the obligation of contract, Congress can do so. The goal of the  
17 Bankruptcy Code is adjusting the debtor-creditor relationship.  
18 Every discharge impairs contracts. While bankruptcy law  
19 endeavors to provide a system of orderly, predictable rules for  
20 treatment of parties whose contracts are impaired, that does not  
21 change the starring role of contract impairment in bankruptcy.

22 It follows, then, that contracts may be impaired in this  
23 chapter 9 case without offending the Constitution. The  
24 Bankruptcy Clause gives Congress express power to legislate  
25 uniform laws of bankruptcy that result in impairment of contract;  
26 and Congress is not subject to the restriction that the Contracts  
27  
28

1 Clause places on states. Compare U.S. CONST. art. I, § 8, cl. 4,  
2 with § 10, cl. 1. Hence, the key premise of the centerpiece of  
3 this lawsuit rests on infirm constitutional ground.

4 The federal bankruptcy power also, by operation of the  
5 Supremacy Clause, trumps the similar contracts clause in the  
6 California state constitution. U.S. CONST. Art. VI, cl. 2; CAL.  
7 CONST. Art. I, § 9 ("A bill of attainder, ex post facto law, or  
8 law impairing the obligation of contracts may not be passed.");  
9 Int'l Bhd. of Elec. Workers, Local 2376 v. City of Vallejo (In re  
10 City of Vallejo), 432 B.R. 262, 268-70 (E.D. Cal. 2010), aff'g,  
11 403 B.R. 72, 76-77 (Bankr. E.D. Cal. 2009). For the same reason,  
12 the plaintiffs' other theories also fall.

13 In sum, even if the plaintiffs' benefits are vested property  
14 interests, the shield of the Contracts Clause crumbles in the  
15 bankruptcy arena.

## 17 II

18 A delicate state-federal relationship of mutual sovereigns  
19 in which the Tenth Amendment looms large provides the framework  
20 for municipal bankruptcy and gives context to this dispute.

### 22 A

23 A pair of chapter 9 provisions honors state-federal balance  
24 by reserving certain state powers and by correlatively limiting  
25 the powers of the federal court: 11 U.S.C. §§ 903 and 904.

1  
2 Section 903 reserves to the state the power to control  
3 political and governmental powers, as well as expenditures:

4 § 903. Reservation of State power to control municipalities

5 This chapter does not limit or impair the power of a  
6 State to control, by legislation or otherwise, a  
7 municipality of or in such State in the exercise of the  
8 political or governmental powers of such municipality,  
9 including expenditures for such exercise, but -

10 (1) a State law prescribing a method of composition of  
11 indebtedness of such municipality may not bind any creditor  
12 that does not consent to such composition; and

13 (2) a judgment entered under such a law may not bind a  
14 creditor that does not consent to such composition.

15 11 U.S.C. § 903.

16 This reservation is limited by the Supremacy Clause. A  
17 state cannot rely on the § 903 reservation of state power to  
18 condition or to qualify, i.e. to "cherry pick," the application  
19 of the Bankruptcy Code provisions that apply in chapter 9 cases  
20 after such a case has been filed. Mission Indep. School Dist. v.  
21 Texas, 116 F. 175, 176-78 (5th Cir. 1940) (chapter IX); Vallejo,  
22 403 B.R. at 75-76; In re City of Stockton, 2012 Westlaw 2905523  
23 at \*4 - \*5 (Bankr. E.D. Cal. 2012) ("Stockton I"); In re Cnty. of  
24 Orange, 191 B.R. 1001, 1021 (Bankr. C.D. Cal. 1996).

25 While a state may control prerequisites for consenting to  
26 permit one of its municipalities (which is an arm of the state  
27 cloaked in the state's sovereignty) to file a chapter 9 case, it  
28 cannot revise chapter 9. Stockton I, at \*4 - \*5. For example,  
it cannot immunize bond debt held by the state from impairment.  
Mission Indep. School Dist., 116 F. at 176-78.

1  
2 Section 904 complements § 903. In view of the inability of  
3 a state to control or condition chapter 9 proceedings after the  
4 municipal case is filed with the state's permission, § 904  
5 imposes limits on the federal court to assure that powers  
6 reserved to the states are honored:

7 § 904 Limitation on jurisdiction and powers of court

8 Notwithstanding any power of the court, unless the  
9 debtor consents or the plan so provides, the court may not,  
10 by any stay, order, or decree, in the case or otherwise,  
11 interfere with -

12 (1) any of the political or governmental powers of the  
13 debtor;

14 (2) any of the property or revenues of the debtor; or

15 (3) the debtor's use or enjoyment of any income-  
16 producing property.

17 11 U.S.C. § 904.

18 As the construction of § 904 is central to the instant  
19 matter, its history is important.

20 The statutory limit on the authority of the court that is  
21 now § 904 has been enacted four times. Each revision has reduced  
22 the latitude within which the court can act. The limit has come  
23 to be described as "absolute."

24 The overall goal is a balance that does not offend the Tenth  
25 Amendment: "The powers not delegated to the United States by the  
26 Constitution, nor prohibited by it to the States, are reserved to  
27 the States, or to the people." U.S. CONST. amend. X.

28 B

The evolution of the limit on court authority in what is now

1 § 904 – from 1934 to its current version – is instructive.  
2 Perceived defects in the limit were a basis for invalidating the  
3 first municipal bankruptcy law as unconstitutional. Ever since,  
4 Congress has keep a weather eye on the constitutionality problem.

5  
6 1

7 The first enactment of the limit on court authority was in  
8 the first municipal bankruptcy law in 1934:

9 The judge ... (11) shall not, by any order or decree,  
10 in the proceeding or otherwise, interfere with (a) any of  
11 the political or governmental powers of the taxing district,  
12 or (b) any of the property or revenues of the taxing  
district necessary in the opinion of the judge for essential  
governmental purposes, or (c) any income-producing property,  
unless the plan of readjustment so provides.

13 Bankruptcy Act § 80(c)(11), Act of May 24, 1934, 48 Stat. 801  
14 (emphasis supplied).

15 The Supreme Court disapproved the 1934 statute as an  
16 unconstitutional interference with the sovereignty of a state on  
17 two theories. First, structurally, municipal bankruptcy was an  
18 impossible contradiction of federalism. Second, the particular  
19 statutory terms might enable the federal government to impose its  
20 will on an unwilling sovereign state. Ashton, 298 U.S. at 532.

21 Although the Bekins Court repudiated Ashton's structural  
22 objection when validating the 1937 municipal bankruptcy act, the  
23 second Ashton rationale has endured and has influenced Congress  
24 always to confine its exercise of the bankruptcy power to  
25 measures that do not usurp state sovereignty.

1  
2 Congress reacted to Ashton in 1937 by reenacting the  
3 municipal bankruptcy provisions with revisions designed to reduce  
4 the opportunity for excessive federal control over state  
5 sovereignty. Act of Aug. 16, 1937, 50 Stat. 653.

6 One significant change was deletion of the phrase "in the  
7 opinion of the judge" so as to make the concept of "property or  
8 revenues necessary for essential services" less dependant on the  
9 subjective view of a federal judge.

10 The revised provision, with that deletion and with shifts in  
11 nomenclature from "taxing district" to "petitioner" and "plan of  
12 arrangement" to "plan of composition," was otherwise unchanged:

13 The judge ... shall not, by any order or decree, in the  
14 proceeding or otherwise, interfere with (a) any of the  
15 political or governmental powers of the petitioner; or (b)  
16 any of the property or revenues of the petitioner necessary  
for essential governmental purposes; or (c) any income-  
producing property, unless the plan of composition so  
provides.

17 Bankruptcy Act § 83(c), Act of Aug. 16, 1937, 50 Stat. 657.

18 The Supreme Court validated the 1937 municipal bankruptcy  
19 statute in Bekins, reasoning that it was a cooperative enterprise  
20 by state and federal sovereigns that was carefully drawn so as  
21 not to infringe state sovereignty. Bekins, 304 U.S. at 51. It  
22 emphasized that a state "retains control of its fiscal affairs"  
23 and that "no control or jurisdiction over that property and those  
24 revenues of the petitioning agency necessary for essential  
25 governmental purposes is conferred" on the federal court. Id.

1  
2 The third version of the statutory limit on court authority  
3 was part of a modernization of former Bankruptcy Act chapter IX  
4 in 1976. Act of Apr. 8, 1976, Pub. L. 94-260, 90 Stat. 315.

5 The statutory limit changed in three important respects.  
6 First, the municipality could consent to exercise of otherwise-  
7 prohibited federal judicial authority. Second, it was clarified  
8 that the limitation applied to stays, including automatic stays.  
9 Third, the qualification "necessary for essential government  
10 services" was deleted from the ban on interference with property  
11 or revenues of the debtor.

12 This 1976 version, new Bankruptcy Act § 82(c), provided:

13 (c) LIMITATION. - Unless the petitioner consents or the  
14 plan so provides, the court shall not, by any stay, order or  
15 decree, in the case or otherwise, interfere with -

16 (1) any of the political or governmental powers of the  
17 petitioner;

18 (2) any of the property or revenues of the petitioner;  
19 or

20 (3) the petitioner's use or enjoyment of any income-  
21 producing property.

22 Bankruptcy Act § 82(c), Act of Apr. 8, 1976, 90 Stat. 316.

23 Congress made plain that it was preserving the strict  
24 limitation on judicial interference with political or  
25 governmental powers, property or revenue, or income-producing  
26 property based on Ashton and Bekins and their progeny: the  
27 Supreme Court and Courts of Appeals have "made it very clear that  
28 the jurisdiction of the court 'is strictly limited to  
disapproving or to approving and carrying out a proposed  
composition.'" The bill follows these holdings and retains the

1 limitation on the court's power." H.R. Rep. No. 94-260, 94th  
2 Cong., 1st Sess., at 9-10, reprinted in 1976 USCCAN at 547-48.<sup>3</sup>

3 The deletion of the phrase "necessary for essential  
4 government services" from § 82(c)(2) aimed to broaden the  
5 limitation. The words "necessary" and "essential" invited  
6 unnecessary litigation. The "governmental services" language  
7 reflected an obsolete distinction between governmental and  
8 proprietary functions that the Supreme Court abolished in 1946.  
9 The phrase overlapped and confused the related ban on judicial  
10 interference with income-producing property.<sup>4</sup>

11 \_\_\_\_\_  
12 <sup>3</sup>And:

13 Subsection (c) repeats and broadens the limitation in  
14 section 83(c), paragraph 1, of current law on the power  
15 granted to the court under subsection (b) and elsewhere in  
16 the chapter, by prohibiting any interference by the court,  
17 by any order or decree, in any of the political or  
18 governmental powers of the petitioner; any of the property  
19 or revenues of the petitioner, or which is used or enjoyed  
20 by the petitioner. The Committee feels that this limitation  
21 is required by Ashton and Bekins [citations omitted], which  
22 defined the limits of Congress' power under the bankruptcy  
23 clause, and the extent to which Congress may grant power to  
24 the courts to assist in the management of the affairs of a  
25 distressed municipality.

26 H.R. Rep. No. 94-260, 94th Cong., 1st Sess., at 18, reprinted in  
27 1976 USCCAN at 556.

28 <sup>4</sup>The House Committee explained:

29 The second change broadens the limitation by eliminating  
30 the phrase "necessary for essential governmental services"  
31 from the second paragraph of the subsection. The phrase was  
32 deleted for three reasons. First, the words "necessary" and  
33 "essential" were conducive to litigation. Second, and more  
34 importantly, the Supreme Court in New York v. United States,  
35 326 U.S. 572, abolished the distinction between governmental  
36 and proprietary functions. Thus, it is now appropriate to

1  
2 The 1976 version was reenacted in 1978 as 11 U.S.C. § 904  
3 with the addition of the preambular phrase "Notwithstanding any  
4 power of the court."

5 This additional limiting language forbids resort to a  
6 federal court's inherent or equitable powers. It reflects  
7 reinvigorated sensitivity in 1978 by Congress to the need to  
8 avoid unnecessary intrusions of state sovereignty in order to  
9 obviate the risk of invalidation by the Supreme Court.

10 That heightened concern stemmed, in part, from the Supreme  
11 Court's then-recent invocation of the Tenth Amendment to  
12 invalidate part of a labor statute. Nat'l League of Cities v.  
13 Usery, 426 U.S. 833, 842-52 (1976), overruled, Garcia v. San  
14 Antonio Metro. Transit Auth., 469 U.S. 528, 531 (1985).

15 Usery worried the drafters of the Bankruptcy Code. The

16  
17 prohibit interference by the court in any of the  
18 municipalities' functions, for they are all equally  
19 governmental functions.

20 Third, the limitation, on interference with any income-  
21 producing property, seems to deprive the qualification  
22 "essential for necessary governmental services" of any  
23 effect. Under one, the court is denied the power to  
24 interfere with property necessary for governmental services;  
25 under the other, the court may not interfere with any  
26 income-producing property. There is conceivably a third  
27 category of property, non-income-producing property that is  
28 not necessary for essential governmental services, but the  
existence of that category does not warrant the potential  
for litigation that exists with the old language. In any  
case, no constitutional problem is anticipated, because the  
power of the court to interfere with the petitioner is  
further limited by the change.

H.R. Rep. No. 94-260, 94th Cong., 1st Sess., at 18, reprinted in  
1976 USCCAN at 556 (footnote omitted).

1 House Committee noted, the "Usery case underlines the need for  
2 this limitation on the court's powers" and added that § 904  
3 "makes clear that the court may not interfere with the choices a  
4 municipality makes as to what services and benefits it will  
5 provide to its inhabitants." H.R. Rep. No. 95-595, at 398. Even  
6 though later overruled, Usery is a reminder that the Tenth  
7 Amendment is a brooding presence over the chapter 9 landscape.

## C

10 The message derived from this history regarding the power of  
11 this court to interfere with the City's actions regarding retiree  
12 health benefits compels the conclusion that § 904 prevents any  
13 federal court from doing what the plaintiffs request, regardless  
14 of whether the City's action is fair or unfair.

15 The concern has constitutional proportions. Chapter 9  
16 passed constitutional muster on the basis that the federal  
17 bankruptcy power be exercised at the request of, but not at the  
18 expense of, the sovereign state in an exercise of cooperation  
19 among sovereigns. Bekins, 304 U.S. at 51-53 (here "we have  
20 coöperation to provide a remedy for a serious condition in which  
21 the States alone were unable to afford relief.").

22 As a state-federal cooperative enterprise conducted in  
23 delicate circumstances in which state sovereignty must be  
24 respected, Congress has been sedulous to assure that the  
25 bankruptcy power not be used in municipal insolvencies in a  
26 manner that oversteps delicate state-federal boundaries.

1 The entire structure of chapter 9 has been influenced by  
2 this pervasive concern to preserve the niceties of the state-  
3 federal relationship. The foundation involves multiple levels of  
4 consent. No chapter 9 case can be filed other than a voluntary  
5 case filed by the municipality with the consent of the state. 11  
6 U.S.C. § 109(c)(2). The municipality consents by filing the  
7 voluntary case. 11 U.S.C. § 301, incorporated by § 901(a).  
8 Consent is implicit in the restriction that only the municipality  
9 can propose a plan of adjustment. 11 U.S.C. § 941. Another  
10 consent is the express consent recognized in § 904 that the City  
11 has declined to give in this proceeding. 11 U.S.C. § 904.

12 Other provisions further the Constitutional restriction  
13 against encroaching on state sovereignty. For example, the  
14 Bankruptcy Code's restrictions on use, sale, or lease of property  
15 do not apply in chapter 9. Compare 11 U.S.C. § 901(a), with id.  
16 § 363. Nor is there provision for a trustee or examiner in a  
17 chapter 9 case. Compare 11 U.S.C. § 901(a), with id. § 1104.

18 In the overall construct, § 904 performs the role of the  
19 clean-up hitter in baseball. Its preambular language  
20 "[n]otwithstanding any power of the court, ... the court may not,  
21 by any stay, order, or decree, in the case or otherwise ..." is  
22 so comprehensive that it can only mean that a federal court can  
23 use no tool in its toolkit - no inherent authority power, no  
24 implied equitable power, no Bankruptcy Code § 105 power, no writ,  
25 no stay, no order - to interfere with a municipality regarding  
26 political or governmental powers, property or revenues, or use or  
27

1 enjoyment of income-producing property. 11 U.S.C. § 904. As a  
2 practical matter, the § 904 restriction functions as an anti-  
3 injunction statute – and more.

4 In short, the § 904 limitation on the court's authority is  
5 absolute, with only the two exceptions stated in § 904: consent;  
6 and provision in a plan of adjustment (which can only be proposed  
7 by the municipality). 6 COLLIER ON BANKRUPTCY ¶ 904.01 (Alan N.  
8 Resnick & Henry J. Sommer eds., 16th ed. 2011) ("COLLIER").  
9

### 10 III

11 The plaintiffs contend that § 904 does not apply and does  
12 not prevent the relief sought. They say they challenge only the  
13 role of the City as employer, not as governmental regulator, and  
14 that neither § 904(1) nor § 904(3) is implicated. While that  
15 argument is weak, § 904(2) is dispositive.  
16

#### 17 A

18 Conceding that the § 904(2) prohibition on interfering with  
19 the debtor's "property or revenues" poses an obstacle, plaintiffs  
20 argue<sup>5</sup> that their relief would be an innocuous preservation of  
21 the status quo that would not directly interfere with City  
22 property or revenues, and would not indirectly interfere with  
23

---

24 <sup>5</sup>Supplemental Brief in Support of Application for Temporary  
25 Restraining Order and Preliminary Injunction or in the  
26 Alternative Relief From Stay, at 3 ("Retirees simply seek an  
27 order to preserve the status quo by prohibiting the City from  
unilaterally modifying Plaintiffs' vested and constitutionally-  
protected right to their earned benefits.").

1 revenues, because the retirees' rights to the health benefit is  
2 fixed and immutable. That argument is not persuasive.

3 Coercively preserving a status quo that entails payment of  
4 money from the City treasury interferes with the City's choice to  
5 suspend such payments. The contents of the City treasury are  
6 "property or revenues" within the meaning of § 904(2).

7 It is impossible to envision how granting the plaintiffs'  
8 prayer for an "order compelling the City to maintain the Retiree  
9 Health Benefit with respect to ARECOS members and Class  
10 Plaintiffs and all other City of Stockton retirees entitled to  
11 the Retiree Health Benefit as of July 1, 2012," and to pay  
12 attorney's fees, would not require the payment of money from the  
13 City's property or revenues. In fact, payment would be required.

14 It follows that the relief sought is barred by § 904(2) as  
15 an interference with the City's "property or revenues."  
16

17 B

18 That a TRO was issued in the Orange County chapter 9 case  
19 does not compel the conclusion that a TRO is permitted here. The  
20 TRO in that case required that certain employees who had  
21 nominally been "permanently" laid off instead be treated as  
22 "temporarily" laid off, and required the parties to meet and  
23 confer to work out their differences. Orange Cnty. Emps. Ass'n  
24 v. Cnty. of Orange (In re Cnty. of Orange), 179 B.R. 177, 185  
25 (Bankr. C.D. Cal. 1995) ("Orange County"). It does not appear  
26 the "property or revenues" were being interfered with; it also  
27

1 was noted that the parties thereafter settled apparently before a  
2 monetary consequence ensued. Id. at 185, n.21.

3 Another distinction is that the Orange County TRO related to  
4 the process of assuming or rejecting unexpired collective  
5 bargaining agreements as § 365 executory contracts. 11 U.S.C.  
6 § 365; NLRB v. Bildisco & Bildisco, 465 U.S. 513, 521-23 (1984)  
7 ("Bildisco"); Orange County, 179 B.R. at 183.

8  
9 1

10 The formal statutory analysis is as follows. The § 365  
11 executory contract provisions apply in chapter 9 cases by virtue  
12 of § 901(a). 11 U.S.C. § 901(a), incorporating id. § 365.

13 Sovereign immunity of a municipality is abrogated as to  
14 § 901. 11 U.S.C. § 106(a)(1).<sup>6</sup> All chapter 1 provisions,  
15 including § 106(a)(1), apply in chapter 9. 11 U.S.C. § 103(f).<sup>7</sup>

16 Since § 901(a) lists sections from chapters other than  
17

18 <sup>6</sup>The section provides, in relevant part:

19 (a) Notwithstanding an assertion of sovereign immunity,  
20 sovereign immunity is abrogated as to a governmental unit to  
21 the extent set forth in this section with respect to the  
22 following:

22 (1) Sections . . . , 901, 922, 926, 928, 929, 944, . . . .

23 11 U.S.C. § 106(a)(1).

24 <sup>7</sup>The section provides:

25 (f) Except as provided in section 901 of this title, only  
26 chapters 1 and 9 of this title apply in a case under such  
27 chapter 9.

27 11 U.S.C. § 103(f).

1 chapters 1 or 9 that apply in chapter 9 cases, including § 365,  
2 it follows that the municipality's sovereign immunity is  
3 abrogated with respect to executory contracts.

4 In other words, the municipality's voluntary act of filing a  
5 chapter 9 case triggers two relevant consequences. First, the  
6 municipality consents, within the meaning of § 904, to  
7 interference by a federal court as to the Bankruptcy Code  
8 provisions that apply in chapter 9 cases. Vallejo, 403 B.R. at  
9 75-76; In re Cnty. of Orange, 191 B.R. at 1021. Second,  
10 sovereign immunity is voluntarily abrogated to the extent  
11 provided in § 106.

12 In short, the naked fact of the issuance of a TRO in Orange  
13 County regarding a § 365 issue did not necessarily offend § 904,  
14 even though the rationale for that TRO seems dubious.<sup>8</sup> The  
15 county consented under § 904 to federal judicial interference in  
16 the form of assessing the merits of § 365 assumption or rejection  
17

18 <sup>8</sup>Orange County has been criticized as implying that a  
19 municipality cannot unilaterally breach collective bargaining  
20 agreements before formal rejection. 6 COLLIER ¶ 901.04[9][a].  
21 While the decision is opaque and the need for a TRO unclear, the  
22 actual terms of the TRO requiring that certain employees laid off  
23 "permanently" be deemed laid off only "temporarily" (the  
24 difference relating to seniority and grievance procedures), and  
25 requiring the parties to meet and confer, did not directly affect  
26 the County treasury. It is consistent with a court controlling a  
27 process preliminary to consideration of the reasonable-efforts-  
28 to-negotiate-voluntary-modification prong of Bildisco test for  
§ 365 rejection, 465 U.S. at 526-27, that applies collective  
bargaining agreements. It is not necessarily inconsistent with  
Bildisco, which permitted contracts to be modified on an interim  
basis, subject to later § 365 review. 465 U.S. at 527-34. Absent  
agreement, such contracts ultimately must be rejected with  
damages dealt with in the claims process or assumed cum onere.

1 of executory contracts and waived its sovereign immunity by  
2 virtue of § 106 regarding executory contracts.

3  
4 2

5 Here, the retiree health benefits are not executory  
6 contracts. Performance does not remain due to some extent on  
7 both sides – there are no reciprocal obligations with performance  
8 due by both parties. Bildisco, 465 U.S. at 522 n.6.

9 The retirees insist they have performed their side of the  
10 bargain: "The City already exercised its political discretion to  
11 provide the Benefit and accepted the full performance by the  
12 Retirees of their services to the City to earn the Benefit."  
13 Supplemental Brief, at 3. And, "Each of the ARECOS members and  
14 Class Plaintiffs have satisfied their obligations under their  
15 respective contracts with the City." Complaint, ¶ 60.

16 Under any definition of a § 365 executory contract, the  
17 plaintiffs' prior full performance means they have no executory  
18 contract. So viewed, the Orange County TRO regarding an  
19 executory contract is inapposite to the question of the effect of  
20 § 904(2) on the City's interim cost cutting.

21 To the contrary, and it is hereby so held, § 904(2) prevents  
22 this court from granting the relief requested in this proceeding.

23  
24 3

25 Plaintiffs' counsel agreed at oral argument that plaintiffs  
26 want the court to impose, by way of its injunctive power, the

27  
28 22

1 equivalent of the provisions of Bankruptcy Code § 1114 relating  
2 to "Payment of insurance benefits to retired employees" in  
3 chapter 11 cases even though § 1114 is not specifically made  
4 applicable in chapter 9 cases. 11 U.S.C. § 1114.

5 Section 1114 was enacted in 1988 to provide procedures and  
6 standards for modifying retiree insurance benefits during a  
7 chapter 11 case. The basic rule for chapter 11 is that retiree  
8 insurance payments must continue to be made timely during the  
9 case unless and until the court approves a modification. 11  
10 U.S.C. § 1114(g). Modification requires compliance with a  
11 prescribed negotiation process and prescribed standards to be  
12 applied by the court. 11 U.S.C. §§ 1114(f) - (h).

13 The retiree insurance benefits provisions were modeled on  
14 § 1113, which was adopted in 1984 following the Supreme Court's  
15 Bildisco decision that collective bargaining agreements are  
16 executory contracts eligible for rejection under § 365 and that  
17 they may be unilaterally rejected or modified before formal  
18 rejection is approved by the court. Bildisco, 465 U.S. at 521-  
19 27. New § 1113 imposed rejection procedures and standards for  
20 chapter 11 cases that were more stringent than the rejection  
21 standards prescribed in Bildisco.

22 But neither § 1113 nor § 1114 is designated in § 901(a) as  
23 applicable in chapter 9 cases. 11 U.S.C. § 901(a) (omitting  
24 § 1113 and § 1114).

25 Contentions that the absence of § 1113 from § 901(a) should  
26 be disregarded as an accident and that courts should apply § 1113  
27  
28

1 in chapter 9, instead of the Bildisco standards, have regularly  
2 been rejected. The judicial consensus is that Bildisco controls  
3 rejection of collective bargaining agreements in chapter 9 cases.  
4 Vallejo, 432 B.R. at 270-72, aff'g Vallejo, 403 B.R. at 77-78;  
5 Orange County, 179 B.R. at 183. This court agrees.

6 The delicate constitutional balance that has loomed large  
7 over municipal bankruptcy ever since Ashton further cautions  
8 against taking liberties to cure perceived legislative mistakes.  
9 In chapter 9, where Congress has been careful to observe the  
10 delicacies of the state-federal relationship, it is particularly  
11 appropriate to leave to Congress, not the courts, the decision to  
12 revise § 901(a). See Vallejo, 432 B.R. at 272.

13 The logic focused on the structure of chapter 9, and the  
14 attendant importance of § 901(a) in the context of Congress  
15 taking care not to overstep the Tenth Amendment constraint,  
16 applies as much to § 1114 as to § 1113. The omission of § 1114  
17 from § 901(a) warrants the conclusion, for the same reasons as  
18 articulated in the Vallejo and Orange County decisions, that  
19 § 1114 does not apply in chapter 9 cases.

20 To be sure, this conclusion appears to leave a gap in  
21 chapter 9 cases in the sense that some retiree insurance benefits  
22 are protected from modification by Bildisco's § 365 rejection  
23 standards because they are included in collective bargaining  
24 agreements, while others are not. In reality, any gap is less  
25 than meets the eye in view of the Bildisco holding that it is not  
26 an unfair labor practice for a debtor unilaterally to modify a  
27  
28

1 collective bargaining agreement during the interval between the  
2 filing of the case and the formal rejection of the executory  
3 contract. Bildisco, 465 U.S. at 527-34. In other words,  
4 regardless of whether the retiree insurance benefit is part of an  
5 executory contract or not, the benefit can be modified or  
6 suspended during the pendency of the case.

7  
8 IV

9 The argument that the City has imposed a plan of adjustment  
10 without meeting fundamental requirements of due process, and in  
11 circumvention of plan confirmation standards, relies on the false  
12 premise that the City's so-called "Pendency Plan" adopted for use  
13 during the chapter 9 case is a plan of adjustment.

14  
15 A

16 The pendency plan is not a plan of adjustment. A formal  
17 plan of adjustment must be filed as such, either with the  
18 petition or at such later time as the court fixes. 11 U.S.C.  
19 § 941. No plan was filed with the petition in this case. No  
20 plan has yet been filed. This court has not yet fixed a time for  
21 filing such a plan. If and when such a plan is filed, the  
22 confirmation of the plan will be considered under the standards  
23 prescribed by the statute. 11 U.S.C. § 943.

24 Rather, the pendency plan is an interim survival mechanism  
25 that enables the financially embarrassed municipality, in the  
26 political and governmental judgment of its governing body, to  
27

1 continue to provide what it deems to be essential governmental  
2 services during the interval between the filing of a chapter 9  
3 case and the confirmation of a plan of adjustment.

4 Suspending payment of various obligations during a case  
5 under the Bankruptcy Code is a routine aspect of the  
6 reorganization process. When the Supreme Court clarified in  
7 Bildisco that it is not an unfair labor practice for a chapter 11  
8 debtor unilaterally to implement changes to a collective  
9 bargaining agreement - i.e. unilaterally to breach it - before  
10 the bankruptcy court acts on a § 365 motion to reject the  
11 contract, it necessarily determined that such unilateral changes  
12 do not offend due process. Bildisco, 465 U.S. at 327-34. The  
13 rationale is that upon filing a chapter 11 case, the debtor  
14 becomes "empowered by virtue of the Bankruptcy Code to deal with  
15 its contracts and property in a manner it could not have done  
16 absent the bankruptcy filing." Id. at 528.

17 Unilaterally-modified contracts are dealt with, as the  
18 Supreme Court explained, through conventional bankruptcy law  
19 provisions that entitle the victim of a breach of a prepetition  
20 obligation to file a proof of claim that will be dealt with in  
21 the ordinary claims process and receive the priority provided by  
22 the Bankruptcy Code. Id. at 530 n.12. It is most unlikely that  
23 the Supreme Court, after having impliedly endorsed the process in  
24 Bildisco, would regard it as inconsistent with due process.

25 This analysis applies in chapter 9 as § 365 applies in  
26 municipality cases. 11 U.S.C. § 901(a), incorporating id. § 365.

1 The plaintiffs have prepetition claims that, under their own  
2 theory of the case, are not executory contracts as they fully  
3 performed their bargains before bankruptcy. As noted, they may  
4 file proofs of claim on account of their retiree health benefits  
5 that will be addressed and valued during the claims adjustment  
6 process. 11 U.S.C. §§ 501-02. In addition, any claim that  
7 appears on the list of creditors that the City must file is  
8 deemed "filed," and hence "allowed," if not listed as disputed,  
9 contingent, or unliquidated. 11 U.S.C. § 925.

10 The plan of adjustment, when it is filed, will be confirmed  
11 only if it meets the pertinent statutory confirmation standards.  
12 11 U.S.C. § 943. The plaintiffs will be entitled to accept or  
13 reject the plan. 11 U.S.C. § 1126(a), incorporated by § 901(a);  
14 Fed. R. Bankr. P. 3018. They also will be entitled to object to  
15 confirmation. Fed. R. Bankr. P. 3020(b).

16 The right to present claims, have them evaluated, to accept  
17 or reject the plan, and to object to confirmation is all the  
18 process that is due.

19  
20 B

21 The real remedy for the plaintiffs lies in participating in  
22 the process of formulating a plan of adjustment. As this court  
23 has previously explained, the lessons of recent chapter 9 cases  
24 teach that successful plans of adjustment are most likely to be  
25 achieved by the parties in interest all coming to the table and  
26 participating in bona fide negotiations. Stockton I, 2012

1 Westlaw 2905523 at \*9. Every issue that is resolved by agreement  
2 will enhance the prospects for a successful plan of adjustment.

3 To that end, the court has appointed a judge as standing  
4 mediator for this case to facilitate a negotiated solution.

5 In short, even if injunctive relief were permitted, this  
6 court is persuaded that injunctive relief is neither necessary  
7 nor appropriate to vindicate the rights of the plaintiffs.

8  
9 V

10 Having concluded that injunctive relief is not available as  
11 a matter of law and, in any event, is not necessary and not  
12 appropriate, the alternative of relief from the automatic stay  
13 under 11 U.S.C. § 362 warrants discussion.

14 The City is correct that plaintiffs' request for stay relief  
15 is procedurally incorrect. Stay relief is a matter of general  
16 interest to all creditors (not merely the parties to this  
17 adversary proceeding) that needs to be presented by motion in the  
18 parent chapter 9 case with appropriate notice. See Fed. R.  
19 Bankr. P. 4001(a) & 9014. If the court were inclined to grant  
20 the relief, it would insist upon procedurally proper notice.

21 Nevertheless, the court is obliged to construe the rules of  
22 procedure so as to secure the just, speedy, and inexpensive  
23 determination of every case and proceeding. Fed. R. Bankr. P.  
24 1001. Here, analysis of why relief from the automatic stay is  
25 not warranted may obviate a subsequent wild goose chase.

26 The logic of plaintiffs' request is that, if the bankruptcy  
27

1 court does not have authority to interfere with the City's  
2 property or revenues by virtue of § 904, then they should be  
3 allowed to go to a forum that does have such authority - i.e.,  
4 the California state courts. Sometimes, as with a personal  
5 injury tort action, that is a good solution. But here it would  
6 be fundamentally at odds with basic policy underlying chapter 9.

7 The core of a chapter 9 case is adjustment of the debtor-  
8 creditor relationship. The plaintiffs here are creditors. They  
9 want two things: a judgment that their health benefit claims are  
10 valid and an order compelling the City to maintain payments for  
11 those benefits. Those issues are central to the debtor-creditor  
12 relationship to be dealt with, along with every other unhappy  
13 creditor, in the collective chapter 9 proceeding.

14 No separate judicial proceeding is needed to determine the  
15 validity of prepetition claims. In this case, a filed proof of  
16 claim will be "deemed allowed" unless someone objects, as will a  
17 claim listed by the City without being designated as disputed,  
18 contingent, or unliquidated. 11 U.S.C. §§ 502(a) & 925.

19 Any objection to a claim will be litigated in this court  
20 under established procedures that honor due process without  
21 extensive and expensive satellite litigation. Fed. R. Bankr. P.  
22 3007. Resort to state court would be wasteful of everyone's  
23 resources and introduce unnecessary delay and confusion.

24 For a plan of adjustment to be confirmed as to a class of  
25 claims that has not accepted the plan, it must be "fair and  
26 equitable" and "not discriminate unfairly." 11 U.S.C.

1 § 1129(b)(1), incorporated by id. § 901(a).

2 If no plan is confirmed, the case must be dismissed in which  
3 event the parties are restored to the prebankruptcy status quo.

4 11 U.S.C. § 349, incorporated by id. § 901(a).

5 As to the question of a state court compelling the City to  
6 pay for benefits during the chapter 9 case, there is another  
7 jurisdictional quandary. All City property, wherever located, as  
8 of the commencement of the case is in the exclusive jurisdiction  
9 of the United States District Court of which this bankruptcy  
10 court is a unit. 28 U.S.C. §§ 151 & 1334(e)(1). This exclusive  
11 jurisdiction could make it difficult to enforce a state-court  
12 order requiring payment, and raises fascinating jurisprudential  
13 complexities that are best left to another day.

14 The timing of payment on account of claims is important to  
15 the plaintiffs. The sooner there is agreement regarding their  
16 treatment in the collective chapter 9 case, the sooner they will  
17 salvage something out of this financial predicament.

18 Accordingly, the bankruptcy policy of favoring a collective  
19 proceeding to work out a comprehensive solution to municipal  
20 insolvency counsels against permitting nonbankruptcy litigation  
21 that would materially interfere with the reorganization process.

22 The request for relief from stay will be denied. If the  
23 request were to be revived, it would have to be presented in a  
24 procedurally correct manner.

25

26

27

28

VI

1  
2 Having established that there will be no TRO, no injunction,  
3 and no relief from the automatic stay, as well as having  
4 established that the claims-adjudication procedure within the  
5 collective chapter 9 case is adequate to establish and vindicate  
6 the legitimate interests of the plaintiffs, the question becomes  
7 what is left of this adversary proceeding?

8 The answer is: nothing is left of the adversary proceeding.

9 The court gave notice that "if this court concludes at or  
10 after the July 23, 2012, hearing that 11 U.S.C. § 904 denies  
11 jurisdiction to any court exercising authority over the chapter 9  
12 case of the Defendant, then this adversary proceeding will be  
13 dismissed on the court's own motion." Order Setting Hearing and  
14 Mandatory Briefing Schedule at 2-3. The phrase "any court"  
15 refers to any federal trial or appellate judge.

16 The § 904 question having been answered with a conclusion  
17 that the court lacks authority, and it being plain that nothing  
18 is left in controversy in this adversary proceeding that is not  
19 more appropriately resolved through conventional bankruptcy  
20 procedures, the adversary proceeding is appropriate to dismiss.

21  
22 VII

23 The final question is whether this court is permitted to  
24 enter an order dismissing the adversary proceeding. The answer  
25 turns on a two-step analysis focused on the subject-matter  
26 jurisdiction statute, 28 U.S.C. § 1334, and then on bankruptcy's  
27

1 judicial administration allocation, 28 U.S.C. § 157.

2  
3 A

4 Since who the plaintiffs are and what they want influences  
5 the analysis at each level, the starting point is to clarify  
6 their status in the bankruptcy case.

7 The plaintiffs are "creditors" who have "claims" against the  
8 debtor. Specifically, a "creditor" includes a person with a  
9 "claim" against the debtor that arose before the order for  
10 relief. 11 U.S.C. § 101(10)(A).<sup>9</sup>

11 The plaintiffs' asserted right to require the City to  
12 continue to pay for health benefits based on their prebankruptcy  
13 contractual rights are "claims." 11 U.S.C. § 101(5).<sup>10</sup>

14  
15 <sup>9</sup>"Creditor" is defined in the Bankruptcy Code:

16 (10) The term "creditor" means -

17 (A) entity that has a claim against the debtor that  
18 arose at the time of or before the order for relief  
concerning the debtor;

19 (B) entity that has a claim against the estate of a  
kind specified in section 348(d), 502(f), 502(g), 502(h) or  
502(i) of this title; or

20 (C) entity that has a community claim.

21 11 U.S.C. § 101(10).

22 <sup>10</sup>"Claim" is defined in the Bankruptcy Code:

23 (5) The term "claim" means -

24 (A) right to payment, whether or not such right is  
reduced to judgment, liquidated, unliquidated, fixed,  
25 contingent, matured, unmatured, disputed, undisputed, legal,  
equitable, secured, or unsecured; or

26 (B) right to an equitable remedy for breach of  
performance if such breach gives rise to a right to payment,  
27 whether or not such right to an equitable remedy is reduced

B

1  
2 Federal subject-matter jurisdiction is founded on 28 U.S.C.  
3 § 1334(b), which confers jurisdiction on the district court over  
4 "all civil proceedings arising under title 11, or arising in or  
5 related to cases under title 11."

6 This bankruptcy court exercises § 1334 jurisdiction as a  
7 "unit" of the district court of which this bankruptcy judge is a  
8 "judicial officer of the district court." 28 U.S.C. § 151.

9 The allocation of authority as between district judges and  
10 bankruptcy judges is governed by 28 U.S.C. § 157. A bankruptcy  
11 judge may "hear and determine" and may "enter appropriate orders  
12 and judgments" in core proceedings. 28 U.S.C. § 157(b)(1).

13 In non-core proceedings that are otherwise "related to" a  
14 case under title 11, a bankruptcy judge may "hear" but not  
15 "determine" the matter, leaving the latter function to a district  
16 judge after considering the bankruptcy judge's proposed findings  
17 and conclusions and reviewing de novo matters to which a party  
18 has timely and specifically objected. 28 U.S.C. § 157(c)(1).<sup>11</sup>

19  
20 \_\_\_\_\_  
21 to judgment, fixed, contingent, matured, unmatured,  
22 disputed, undisputed, secured, or unsecured.

23 11 U.S.C. § 101(5).

24 <sup>11</sup>That provision is:

25 (c)(1) A bankruptcy judge may hear a proceeding that is  
26 not a core proceeding but that is otherwise related to a  
27 case under title 11. In such proceeding, the bankruptcy  
28 judge shall submit proposed findings of fact and conclusions  
of law to the district court, and any final order or  
judgment shall be entered by the district judge after  
considering the bankruptcy judge's proposed findings and

1 The parties, however, may consent to have a bankruptcy judge  
2 "hear and determine" such a proceeding.

3 The court has an independent duty to determine the core/non-  
4 core status of a proceeding and is not bound by allegations of  
5 the parties. 28 U.S.C. § 157(b)(3).<sup>12</sup>

## C

8 Starting with subject-matter jurisdiction, the problem is  
9 which category of § 1334(b): "arising under" title 11; "arising  
10 in" a case under title 11; or "related to" cases under title 11.

11 The plaintiffs' allegation that this action is "related to"  
12 a case under title 11 is presented as a naked conclusion with no  
13 facts in support. The syntax of § 1334(b) appears to make the  
14 "related to" category a residual catchall to include matters that  
15 are not necessarily part of the bankruptcy case. But the fringes  
16 of this category have led to considerable litigation. 1 COLLIER  
17 ¶ 3.01[3][e][ii]. The tendency to overuse this category has been

---

18  
19 conclusions and after reviewing de novo those matters to  
20 which any party has timely and specifically objected.

21 28 U.S.C. § 157(c)(1).

22 <sup>12</sup>That duty is:

23 (3) The bankruptcy judge shall determine, on the judge's  
24 own motion or on timely motion of a party, whether a  
25 proceeding is a core proceeding under this subsection or is  
26 a proceeding that is otherwise related to a case under title  
27 11. A determination that a proceeding is not a core  
28 proceeding shall not be made solely on the basis that its  
resolution may be affected by State law.

28 U.S.C. § 157(b)(3).

1 criticized. See Ralph Brubaker, On the Nature of Federal  
2 Bankruptcy Jurisdiction: A General Statutory and Constitutional  
3 Theory, 41 WM. & MARY L. REV. 743, 862-920 (2000) (arguing "related  
4 to" category is narrower than commonly assumed). Now that waters  
5 are roiling in the wake of Stern v. Marshall, 131 S.Ct. 2594  
6 (2011), interests of efficient judicial administration make it  
7 important to focus carefully on the § 1334(b) categories.

8 In this adversary proceeding, the counts in the complaint  
9 assert rights against the City under nonbankruptcy law that might  
10 be considered in a court of general jurisdiction, but the reality  
11 is that this action would not exist in the absence of this  
12 chapter 9 case. Without the federal bankruptcy power to impair  
13 contracts, the City's unilateral reduction of retiree health  
14 benefits would not be attempted in the first place. In other  
15 words, but for the existence of this chapter 9 case, there would  
16 be no justiciable dispute. It follows that this dispute is too  
17 close to the heart of the bankruptcy case to be regarded as  
18 merely "related to" a case under title 11. The jurisdictional  
19 allegation in the complaint is rejected as incorrect.

20 The question then becomes whether this dispute "arises under  
21 title 11" or "arises in a case under title 11."

22 The "arising under" § 1334(b) category has heretofore been  
23 understood to mean causes of action that are created by the  
24 Bankruptcy Code. 1 COLLIER ¶ 3.01[3][e][i]. The difficulty here  
25 is that under the conventional view, the complaint does not  
26 invoke bankruptcy law; the Bankruptcy Code involvement occurs  
27  
28

1 when § 904 swoops in from nowhere-mentioned-in-the-complaint to  
2 bar the injunction. While the City's unilateral interim action  
3 is permitted to occur during a bankruptcy case, title 11 does not  
4 specifically authorize the interim action. Nor are any of the  
5 plaintiffs' causes of action created by title 11. In these  
6 circumstances, the fit with the "arising under" category is  
7 uncomfortable; the "arising in" category may be the better fit.

8 1 COLLIER ¶ 3.01[3][e][iv].

9 The third § 1334(b) category is the proceeding "arising in"  
10 a case under title 11. The parameters of this intermediate  
11 category have been poorly outlined in the case law and deserve  
12 more careful attention. It is argued in the academic literature  
13 that, based on historical jurisprudence, more cases qualify as  
14 "arising in" a case under title 11 than commonly assumed.

15 Brubaker, 41 WM. & MARY L. REV. at 755, 859-62, 914 n.599.

16 Regardless of whether the outer dimensions of § 1334(b)  
17 "arising in" jurisdiction may be uncertain, existing case law  
18 discerns such jurisdiction as including proceedings that, while  
19 not based on a right created by title 11, would not exist outside  
20 of bankruptcy. Harris v. Wittman (In re Harris), 590 F.3d 730,  
21 737 (9th Cir. 2009); Maitland v. Mitchell (In re Harris Pine  
22 Mills, Inc.), 44 F.3d 1431, 1434 (9th Cir. 1995); Eastport  
23 Assocs. v. City of Los Angeles (In re Eastport Assocs.), 935 F.2d  
24 1071, 1076 (9th Cir. 1991); Wood v. Wood (In re Wood), 825 F.2d  
25 90, 97 (5th Cir. 1987); Menk v. LaPaglia (In re Menk), 241 B.R.  
26 896, 909 (9th Cir. BAP 1999). It is sometimes said that "arising  
27  
28

1 in" relates to the "administration" of the case. E.g. Wood, 825  
2 F.2d at 97; 1 COLLIER ¶ 3.01[3][e][iv].

3 Here, the plaintiff creditors allege nonbankruptcy theories  
4 to attack interim measures regarding their claims taken under the  
5 authority of bankruptcy law in the course of administration of  
6 the case. The basis of the injunction complaint involves the  
7 debtor-creditor relationship between the parties and calls into  
8 question the enforceability of bankruptcy doctrines. Such a  
9 dispute comfortably fits within the established judicial  
10 construction of the § 1334(b) "arises in" category. 28 U.S.C.  
11 § 1334(b); Harris, 590 F.3d at 737-38; Menk, 241 B.R. at 909. It  
12 is also sufficient (but not necessary) that the outcome is  
13 affected by a section of the Bankruptcy Code – § 904.

14 Accordingly, this proceeding "arises in" a case under title  
15 11, within the meaning of 28 U.S.C. § 1334(b).

16  
17 D.

18 The next task is to determine whether the proceeding  
19 qualifies as a core proceeding. Sixteen examples of core  
20 proceedings are listed at 28 U.S.C. § 157(b)(2)(A)-(P). The list  
21 is not limiting. 11 U.S.C. § 102(3); 1 COLLIER ¶ 3.02[3]. As the  
22 definitions overlap and are nonexclusive, the sixteen categories  
23 are not mutually exclusive and fall into five general categories:  
24 (1) matters of administration; (2) avoidance actions; (3) matters  
25 concerning property of the estate; (4) omnibus categories; and  
26 (5) chapter 15 cases. 1 COLLIER ¶ 3.02[3][a]. The first and  
27  
28

1 fourth categories are implicated in this instance.

2 This lawsuit is a core proceeding on three adequate,  
3 independent grounds: §§ 157(b)(2)(A), (B), and (O).

4 Since the gravamen of the complaint challenges interim  
5 actions being taken by the City in the course of administering  
6 the case, it qualifies as a core proceeding on that basis. 28  
7 U.S.C. § 157(b)(2)(A); 1 COLLIER ¶ 3.02[3][a].

8 The determination that the plaintiffs are "creditors" who  
9 have "claims" against the debtor implicates core proceeding  
10 status regarding "allowance or disallowance of claims" of  
11 creditors. 28 U.S.C. § 157(b)(2)(B). Thus, the demand for a  
12 declaratory judgment that plaintiffs have a vested property  
13 interest is merely a premature request that this court determine  
14 that their claims are allowed; this is the essential routine of  
15 the claims administration process.

16 Finally, this chapter 9 involves the adjustment of financial  
17 relations between the City and all of its creditors, including  
18 the plaintiffs, in a process that will culminate in a chapter 9  
19 plan of adjustment. As such, this proceeding that focuses on the  
20 relationship between debtor City and creditor plaintiffs is a  
21 core proceeding as an "other proceeding" affecting the  
22 "adjustment of the debtor-creditor or the equity security holder  
23 relationship." 28 U.S.C. § 157(b)(2)(O); Harris, 530 F.3d at  
24 738-40; 1 COLLIER ¶ 3.02[3][d][ii].

25 Therefore, this entire dispute is a "core proceeding" that  
26 "arises in" this chapter 9 case that a bankruptcy judge may "hear  
27  
28

1 and determine" and "enter appropriate orders and judgments"  
2 pursuant to 28 U.S.C. § 157(b) (1).

3 The appropriate order in this instance is an order  
4 dismissing this adversary proceeding. The dismissal will be  
5 without prejudice to further prosecution of the plaintiffs'  
6 claims in the routine course of the reorganization and claims  
7 administration process, which process does not ordinarily require  
8 an adversary proceeding.

9  
10 Conclusion

11 For the reasons stated, Bankruptcy Code § 904 forbids the  
12 injunction requested. Settled bankruptcy law permits the City to  
13 implement interim contractual modifications before the  
14 confirmation of a chapter 9 plan of adjustment but such revisions  
15 do not, as a matter of law, become permanent unless and until  
16 made part of a confirmed plan of adjustment or otherwise  
17 voluntarily agreed. The plaintiffs' substantive claims will be  
18 more expeditiously fixed and determined in accordance with  
19 principles of due process without the need for this adversary  
20 proceeding. Stay relief is inappropriate because the nature of  
21 the dispute is integral to the adjustment of the debtor-creditor  
22 relationship that policy dictates occur in a single forum.

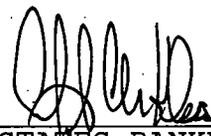
23 The remedy for the plaintiffs is to participate in the  
24 process of negotiating their treatment under a chapter 9 plan.

25 This is a core proceeding that "arises in" the chapter 9  
26 case and would not exist "but for" the chapter 9 case.

1 Accordingly, orders will be entered DENYING the motion for  
2 TRO and preliminary injunction and declining to afford relief  
3 from the automatic stay.

4 This adversary proceeding will be DISMISSED, without  
5 prejudice to the prosecution by the plaintiffs of their various  
6 claims through conventional bankruptcy procedure.

7 Dated: August 6, 2012.



8  
9 UNITED STATES BANKRUPTCY JUDGE

10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

**CERTIFICATE OF SERVICE**

On the date indicated below, I served a true and correct copy(ies) of the attached document by placing said copy(ies) in a postage paid envelope addressed to the person(s) hereinafter listed and by depositing said envelope in the United States mail or by placing said copy(ies) into an interoffice delivery receptacle located in the Clerk's Office.

Marc A. Levinson  
400 Capitol Mall #3000  
Sacramento CA 95814-4407

Office of the U.S. Trustee  
Robert T Matsui United States Courthouse  
501 I Street, Room 7-500  
Sacramento CA 95814

Jerrold E. Abeles  
555 W 5th St 48th Fl  
Los Angeles CA 90013

Steven H. Felderstein  
400 Capitol Mall #1450  
Sacramento CA 95814-4434

Christina M. Craige  
555 W 5th St #4000  
Los Angeles CA 90013

Alan C. Geolot  
1501 K St NW  
Washington DC 20005

Guy S. Neal  
1501 K St NW  
Washington DC 20005

Michael M. Lauter  
4 Embarcadero Ctr 17th Fl  
San Francisco CA 94111-4109

Robert S. McWhorter  
621 Capitol Mall, 25th Floor  
Sacramento CA 95814

Allan H. Ickowitz  
777 S. Figueroa Street, 34th Floor  
Los Angeles CA 90017

Roberto J. Kampfner  
633 West Fifth Street Suite 1900  
Los Angeles CA 90071

James O. Johnston  
555 S Flower St 50th Fl  
Los Angeles CA 90071

Scott H. Olson  
560 Mission Street, Suite 3100  
San Francisco CA 94105

William A. Van Roo  
13863 Quaterhorse Dr.  
Grass Valley CA 95949

Richard A. Lapping  
101 California Street, Ste. 3900  
San Francisco CA 94111

Lawrence A. Larose  
200 Park Ave  
New York NY 10166-4193

Sarah L. Trum  
1111 Louisiana 25th Fl  
Houston TX 77002

Donna T. Parkinson  
400 Capitol Mall Suite 2560  
Sacramento CA 95814

David E. Mastagni  
1912 I St  
Sacramento CA 95811

Robert B. Kaplan  
2 Embarcadero Center 5th Fl  
San Francisco CA 94111-3824

Nicholas DeLancie  
Two Embarcadero Center, 5th Floor  
San Francisco CA 94111

John A. Vos  
1430 Lincoln Ave  
San Rafael CA 94901

Jeffry A. Davis  
44 Montgomery St 36th Fl  
San Francisco CA 94104

Abigail V. O'Brient  
3580 Carmel Mountain Rd #300  
San Diego CA 92130

William W. Kannel  
1 Financial Center  
Boston MA 02111

George S. Emblidge  
220 Montgomery St #2100  
San Francisco CA 94104

Dated: 8/6/12



DEPUTY CLERK