

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

FOR PUBLICATION

FILED July 13, 2012

THIS IS A REPLICA OF THE FILED DOCUMENT
PROVIDED IN TEXT SEARCHABLE FORMAT.
THE ORIGINAL IS AVAILABLE ON PACER.

UNITED STATES BANKRUPTCY COURT EASTERN
DISTRICT OF CALIFORNIA

**UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA**

In re:) Case No. 12-32118-C-9
)
CITY OF STOCKTON, CALIFORNIA,) DC No. OHS-4
)
)
Debtor(s).)
_____)

**OPINION
ON MOTION FOR LEAVE TO INTRODUCE EVIDENCE
RELATING TO NEUTRAL EVALUATION PROCESS UNDER
CALIFORNIA GOVERNMENT CODE § 53760.3(q)**

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

CHRISTOPHER M. KLEIN, Chief Bankruptcy Judge:

This case of first impression involves the boundaries, the
interplay, and the common ground between federal law and state
law in the context of the confidentiality requirement in
California's new statute channeling a municipality through a
neutral evaluation process before filing a chapter 9 case to
adjust debts under the U.S. Bankruptcy Code.

Upon filing this chapter 9 case, the City of Stockton filed
the instant motion invoking the part of California Government
Code § 53760.3(q) that authorizes a bankruptcy judge to lift the
shroud of confidentiality from the pre-filing neutral evaluation

1 for the limited purpose of establishing the City's eligibility
2 for chapter 9 relief. This court accepts the invitation only
3 with respect to the one chapter 9 eligibility element for which
4 state law provides the rule of decision and otherwise declines
5 because state evidence law does not govern evidence in federal
6 court on issues when federal law provides the rule of decision.

7 Nevertheless, federal policy encouraging settlement also
8 favors preserving confidentiality of compromise discussions and
9 permits federal trial judges to ration the disclosure of
10 confidential settlement discussions on their own authority.
11 Hence, this court will impose a confidentiality protective order
12 and take an incremental approach to disclosure as there is no
13 indication in the case as yet that detailed evidence of
14 confidential discussions will be needed in order to determine
15 chapter 9 eligibility.

16 17 Facts

18 The City of Stockton, California, filed this chapter 9 case
19 on June 28, 2012, following the conclusion of the newly-enacted
20 pre-filing neutral evaluation required by California Government
21 Code § 53760 as a precondition for permitting a California
22 municipality to file a chapter 9 case.

23 The next day, the City filed this Emergency Motion For Leave
24 To Introduce Evidence Relating To Neutral Evaluation Process
25 Under Government Code § 53760.3(q) seeking permission to
26 introduce evidence as to: (1) the number and length of meetings
27 between the City and its creditors; (2) the identity of the

1 participants at such meetings; (3) the types of issues discussed;
2 (4) the financial and other information shared; (5) the offers
3 exchanged and the discussions between the parties; and (6) the
4 status of negotiations between the City and each interested party
5 as of the petition date.

6 Oral argument was entertained in open court on July 6, 2012.
7 This decision memorializes the ruling made from the bench at the
8 end of that hearing.

9 10 Analysis

11 Context matters. Here, what is going on is the process of
12 determining whether to enter an order for relief, which is the
13 initial judicial task in every chapter 9 case. We begin with an
14 inventory of the essential elements for chapter 9 eligibility and
15 how one goes about determining them, before assessing the effect
16 of Government Code § 53760 on this chapter 9 case.

17 18 I

19 Chapter 9 is peculiar in that the filing of a voluntary
20 petition does not constitute an order for relief. 11 U.S.C.
21 § 921(d). Rather, the municipality must be prepared to litigate
22 its way to an order for relief in its voluntary case by
23 demonstrating its eligibility to be a chapter 9 debtor and
24 establishing that it filed the petition in good faith. 11 U.S.C.
25 §§ 109(c) & 921(c).

26 A

27 Five essential elements for eligibility to be a chapter 9
28

debtor are set forth at 11 U.S.C. § 109(c), to which is appended a good faith filing requirement by 11 U.S.C. § 921(c). 2 COLLIER ON BANKRUPTCY ¶ 109.04 (Alan N. Resnick & Henry J. Sommer eds. 16th ed. 2011) ("COLLIER").

First, there must be a "municipality," which is defined as a "political subdivision or public agency or instrumentality of a State." 11 U.S.C. §§ 101(40) & 109(c)(1); 2 COLLIER ¶ 109.04[3][a].

Second, the municipality must be specifically authorized, in its capacity as a municipality or by name, to be a debtor under chapter 9 by state law, or by a governmental officer or organization empowered by state law to authorize such entity to be a debtor under such chapter. 11 U.S.C. § 109(c)(2); 2 COLLIER ¶ 109.04[3][b].

Third, the municipality must be "insolvent," which is specially defined for chapter 9 purposes as "(i) generally not paying its debts as they become due unless such debts are the subject of a bona fide dispute; or (ii) unable to pay its debts as they become due." 11 U.S.C. §§ 101(32)(C) & 109(c)(3); 2 COLLIER ¶ 109.04[3][c].

Fourth, the municipality must desire to effect a plan to adjust the debts it is generally not paying or unable to pay. 11 U.S.C. § 109(c)(4); 2 COLLIER ¶ 109.04[3][d].

Fifth, a creditor negotiation requirement may be satisfied by one of four alternatives. The municipality must have: (A) obtained the agreement of creditors holding at least a majority in amount of the claims of each class that it intends to impair

1 under a chapter 9 plan; or (B) negotiated in good faith with
2 creditors and have failed to obtain the agreement of creditors
3 holding at least a majority in amount of the claims of each class
4 that it intends to impair under a chapter 9 plan; or (C) be
5 unable to negotiate with creditors because such negotiation is
6 impracticable; or (D) reasonably believe that a creditor may
7 attempt to obtain a transfer that is avoidable as a preference.
8 11 U.S.C. § 109(c)(5); 2 COLLIER ¶ 109.04[3][e].

9 Here, the City relies on the good-faith negotiation prong at
10 § 109(c)(5)(B) of the creditor negotiation requirement.

11 If the five essential elements are satisfied, then the court
12 must order relief unless the debtor did not file the petition in
13 good faith. Thus, this latter "good faith filing" element can be
14 regarded as a sixth essential element for chapter 9 relief in the
15 sense that relief will not be ordered if the case was not filed
16 in good faith. Compare 11 U.S.C. § 921(c), with id. § 921(d).

17
18 B

19 The burden of proof, at least as to the five § 109(c)
20 elements, is on the municipality as the proponent of voluntary
21 relief.¹ Int'l Assn. of Firefighters, Local 1186 v. City of
22 Vallejo (In re City of Vallejo), 406 B.R. 280, 289 (9th Cir. BAP

24 ¹Given that the City is relying in this instance on the
25 good-faith negotiation prong of § 109(c)(5)(B), debate about who
26 has the good-faith filing burden under § 921(c) can safely be
27 left to another day as it seems improbable (but not impossible)
that good-faith negotiations would precede a filing that is made
not in good faith.

1 2009) ("Vallejo"); In re Valley Health Sys., 383 B.R. 156, 161
2 (Bankr. C.D. Cal. 2008) ("Valley Health"); In re County of
3 Orange, 183 B.R. 594, 599 (Bankr. C.D. Cal. 1995) ("Orange
4 County"); 2 COLLIER ¶ 109.04[2].

5 The quantum of proof, there being no contrary indication in
6 statute or in controlling decisional law, is the familiar
7 preponderance-of-evidence standard of basic civil litigation.
8 Nothing suggests there should be a higher burden. This
9 conclusion comports with the argument by the authors of the
10 Collier treatise that the burden should be liberally applied in
11 favor of granting relief. 2 COLLIER ¶ 109.04[3].

12 Clarifying that the quantum of the burden is preponderance
13 of evidence matters in the present instance because the logic
14 behind the breadth of the City's request to dispense with
15 confidentiality of the pre-filing neutral evaluation appears to
16 rest on the incorrect premise that the City will be subjected to
17 some higher standard of proof than preponderance of evidence.

18
19 C

20 The procedure for resolving the eligibility question
21 resembles ordinary federal civil litigation. The petition and
22 supporting materials function as the equivalent of a complaint
23 and objections to the petition as the answer. Material factual
24 disputes will be resolved by way of trial.

25 Once the petition is filed, notice of commencement of the
26 case must be published for three consecutive weeks in a newspaper
27 of general circulation within the district and a newspaper of

1 general circulation among bond dealers and bondholders. 11

2 U.S.C. § 923. One purpose of such notice is to alert parties in
3 interest to the opportunity to "object" to the petition.

4 The court resolves objections to the petition by following a
5 notice and hearing procedure. 11 U.S.C. §§ 921(c)-(d).

6 By process of elimination, the relevant procedure is the
7 Rule 9014 "contested matter." Fed. R. Bankr. P. 9014. Although
8 the notice-and-hearing requirement of § 921(c) puts the question
9 of the order for relief into a litigation context, the Federal
10 Rules of Civil Procedure do not directly specify a procedure for
11 chapter 9 cases. Neither the contested petition provisions of
12 Rules 1011 and 1018 nor the adversary proceeding rule apply in
13 chapter 9. What remains is the Rule 9014 "contested matter"
14 procedure.

15 Under Rule 9014, aside from the absence of formal pleadings,
16 most of the adversary proceeding rules apply. Fed. R. Bankr. P.
17 9014(c). Testimony of witnesses in any disputed material factual
18 issue in a contested matter must be taken in the same manner as
19 testimony in an adversary proceeding - in other words, a fact-
20 based contest in a contested matter is to be resolved by way of
21 trial. Fed. R. Bankr. P. 9014(d).

22 As the petition and supporting documents function as a
23 complaint to place before the court the allegations and factual
24 basis for relief, it is appropriate that facts be alleged with
25 respect to each essential element sufficient to make plausible
26 the proposition that the City is entitled to an order for relief.
27 In other words, at least a prima facie case needs to be stated.

Indeed, the City urges that its need to assert a plausible case as to each essential element for eligibility justifies dispensing with all of the confidentiality protecting the pre-filing neutral evaluation discussions. As will be explained, however, a more incremental approach is appropriate.

The actual nature and extent of the litigation and the increments of disclosure will depend upon the issues that are actually joined by way of objection to the petition. If there are no objections, then the court will be entitled (but not required) to rely on the prima facie case as a basis for ordering relief. If there are objections, a trial will ensue, the complexion of which will depend upon the nature of the dispute and may trigger broader disclosure of pre-filing discussions.

II

The state is the chapter 9 gatekeeper by virtue of § 109(c)(2). But that gatekeeping function ends once the gate is opened and a chapter 9 case is filed.

1 A

2 The gate is the requirement that a municipality is eligible
3 to be a debtor in a chapter 9 case only if it is specifically
4 authorized by state law, or by a governmental officer or
5 organization empowered by state law to authorize the municipality
6 to be a debtor under chapter 9. 11 U.S.C. § 109(c)(2).

7 California has engineered the parameters of its gate in
8 California Government Code § 53760, which authorizes any county,
9 city, district, public authority, public agency, or entity that
10 qualifies as a municipality under the Federal Bankruptcy Code,
11 other than a school district,² to be a debtor under chapter 9 but
12 recently imposed preconditions for which this case functions as
13 the maiden voyage. The municipality must either engage in a
14 neutral evaluation process for a specified period or its
15 governing board must declare a fiscal emergency pursuant to
16 specified procedures. CAL. GOVT. CODE § 53760.³

17
18 ²The statute applies to any "local public entity," which is
19 defined as:

20 (f) "Local public entity" means any county, city,
21 district, public authority, public agency, or other entity,
22 without limitation, that is a municipality as defined in
23 Section 101(40) of Title 11 of the United States Code
(bankruptcy), or that qualifies as a debtor under any other
federal bankruptcy law applicable to local public entities.
For purposes of this article, "local public entity" does not
include a school district.

24 CAL. GOVT. CODE § 53760.1(g).

25 ³The basic authorization is:

26 A local public entity in this state may file a petition
27 and exercise powers pursuant to applicable federal

1 B

2 If the neutral evaluation process concludes without having
3 resolved all pending disputes with creditors, the municipality
4 may file a chapter 9 petition. CAL. GOVT. CODE § 53760.3(u).⁴

5 The municipality and all interested parties participating in
6 the neutral evaluation process have a duty to negotiate in good
7 faith. CAL. GOVT. CODE § 53760.3(o).

8 The parties must maintain the confidentiality of the neutral
9 evaluation process and "not disclose statements made, information
10 disclosed, or documents prepared or produced, during the neutral
11 evaluation process, at the conclusion of the neutral evaluation
12 process," or during any bankruptcy proceeding except upon
13

14 bankruptcy law if either of the following apply:

15 (a) The local public entity has participated in a neutral
16 evaluation process pursuant to Section 53760.3.

17 (b) The local public entity declares a fiscal emergency
18 and adopts a resolution by a majority vote of the governing
19 board pursuant to Section 53760.5.

18 CAL. GOVT. CODE § 53760, as amended by Assembly Bill 506, approved
19 by Governor, October 9, 2011, effective January 1, 2012.

20 ⁴The statute provides:

21 (u) If the 60-day time period for neutral evaluation has
22 expired, including any extension of the neutral evaluation
23 past the initial 60-day time period pursuant to subdivision
24 (r), and the neutral evaluation is complete with differences
25 resolved, the neutral evaluation shall be concluded. If the
26 neutral evaluation process does not resolve all pending
disputes with creditors the local public entity may file a
petition and exercise powers pursuant to applicable federal
bankruptcy law if, in the opinion of the governing board of
the local public entity, a bankruptcy filing is necessary.

27 CAL. GOVT. CODE § 53760.3(u).

1 agreement of all parties or, for the limited purpose of
2 determining chapter 9 eligibility under § 109(c), upon permission
3 of the bankruptcy judge. CAL. GOVT. CODE § 53760.3(q).⁵

4 5 III

6 The question becomes the extent to which the California
7 confidentiality provision applies in the conduct of this chapter
8 9 case and, to the extent it does not apply, how to deal with
9 matters warranting confidentiality.

10 11 A

12 A chapter 9 case is, by definition, a federal proceeding in
13 a federal court. One particular consequence is that the Federal
14 Rules of Evidence apply to this bankruptcy case. E.g., Fed. R.
15 Evid. 1101(b).

16
17 ⁵The precise statutory language is:

18 (q) The parties shall maintain the confidentiality of the
19 neutral evaluation process and shall not disclose statements
20 made, information disclosed, or documents prepared or
21 produced during the neutral evaluation process, at the
22 conclusion of the neutral evaluation process or during any
23 bankruptcy proceeding unless either of the following occur:

24 (1) All persons that conduct or otherwise participate in
25 the neutral evaluation expressly agree in writing, or orally
26 in accordance with Section 1118 of the Evidence Code, to
disclosure of the communication, document, or writing.

27 (2) The information is deemed necessary by a judge
28 presiding over a bankruptcy proceeding pursuant to Chapter 9
of Title 11 of the United States Code to determine
eligibility of a municipality to proceed with a bankruptcy
proceeding pursuant to Section 109(c) of Title 11 of the
United States Code.

29 CAL. GOVT. CODE § 53760.3(q).

1 With respect to privileges – and California's
2 confidentiality requirement arguably in the nature of a privilege
3 under California Evidence Code § 1119⁶ – the controlling federal
4 provision is Federal Rule of Evidence 501:

5 Rule 501. Privilege in General

6 The common law – as interpreted by United States courts
7 in the light of reason and experience – governs a claim of
8 privilege unless any of the following provides otherwise:

- 9 ● the United States Constitution;
- 10 ● a federal statute; or
- 11 ● rules prescribed by the Supreme Court.

12 But in a civil case, state law governs privilege
13 regarding a claim or defense for which state law supplies
14 the rule of decision.

15 Fed. R. Evid. 501.

16 The rules on privilege apply to all stages of this chapter 9
17 case. Fed. R. Evid. 1101(c).

18 It follows that the confidentiality provision of California
19 Government Code § 53760.3(q) apply only to the extent that this
20 bankruptcy court confronts a question governed by a state rule of
21 decision.

22 In the context of chapter 9 eligibility, state law provides
23 the rule of decision only for § 109(c)(2): whether the entity
24 "is specifically authorized, in its capacity as a municipality or
25 by name, to be a debtor under such chapter by State law, or by a
26 governmental officer or organization empowered by State law to
27 authorize such entity to be a debtor under such chapter;[.]"

28 Indeed, § 109(c)(2) presents a question of pure state law.
Under that provision, it has been determined as a matter of New

⁶Cf. Government Code § 53760.3(q) (specifically
incorporating Cal. Evid. Code § 1118).

1 York State constitutional law that the Governor of New York had
2 the authority to authorize an entity to file a chapter 9 case.
3 In re N.Y.C. Off-Track Betting Corp., 427 B.R. 256, 264 (Bankr.
4 S.D.N.Y. 2010). By the same token, nothing in New York law
5 empowered the Suffolk County (N.Y.) Legislature to authorize a
6 chapter 9 filing. In re Suffolk Regional Off-Track Betting
7 Corp., 462 B.R. 397, 414-21 (Bankr. E.D.N.Y. 2011).

8 Here, California constructed its own gate at the entrance to
9 the chapter 9 arena and is entitled to have it construed as a
10 matter of state law.

11 All other eligibility questions under § 109(c) – § 109(c)(1)
12 municipality; § 109(c)(3) insolvent; § 109(c)(4) desire to effect
13 plan of adjustment; and § 109(c)(5) creditor negotiation – and
14 the good faith question under § 921(c) are federal questions
15 based on, and created by, the federal Bankruptcy Code and subject
16 to a federal rule of decision as to which the California
17 confidentiality provision does not control.

18 In short, the only portion of California Government Code
19 § 53760.3(q) that applies to the chapter 9 eligibility analysis
20 in this instance is the question whether the City complied with
21 the neutral evaluation requirement.

22
23 B

24 Having concluded that the California statutory
25 confidentiality requirement applies to § 109(c)(2), but only to
26 § 109(c)(2), the focus shifts to what the City wants permission
27 to disclose, which begins with a focus on the precise terms and

1 meaning of the confidentiality statute in order to ascertain what
2 is and is not protected.

3 The terms of California Government Code § 53760.3(q) provide
4 (with the critical terms emphasized):

5 (q) The parties shall maintain the confidentiality of the
6 neutral evaluation process and shall not disclose statements
7 made, information disclosed, or documents prepared or
8 produced during the neutral evaluation process, at the
9 conclusion of the neutral evaluation process or during any
10 bankruptcy proceeding unless either of the following occur:

11 (1) All persons that conduct or otherwise
12 participate in the neutral evaluation expressly agree
13 in writing, or orally in accordance with Section 1118
14 of the Evidence Code, to disclosure of the
15 communication, document, or writing.

16 (2) The information is deemed necessary by a judge
17 presiding over a bankruptcy proceeding pursuant to
18 Chapter 9 of Title 11 of the United States Code to
19 determine eligibility of a municipality to proceed with
20 a bankruptcy proceeding pursuant to Section 109(c) of
21 Title 11 of the United States Code.

22 CAL. GOVT. CODE § 53760.3(q) (emphases supplied).

23 The important question relates to the meaning of the phrase
24 "maintain the confidentiality of the neutral evaluation process."
25 It is noteworthy that the remainder of the section refers only to
26 specific categories of statements, communications, information,
27 and documents and is followed by a temporal clause extending the
28 protection beyond the conclusion of the neutral evaluation
process. Further, the part that provides that all parties can
agree to disclosure of communications, documents, or writings
says nothing about the process itself. CAL. GOVT. CODE
§ 53760.3(q)(1).

29 The analysis is informed by two findings made by the
30 California legislature in Assembly Bill 506 ("AB 506"), which
31 enacted the amendments to Government Code § 53760 creating the

1 neutral evaluation process. First, it found that "allowing the
2 interested parties to exchange information in a confidential
3 environment with the assistance and supervision of a neutral
4 evaluator" assists in determining whether obligations can be
5 renegotiated on a consensual basis.⁷ Second, it made findings
6 designed to excuse the neutral evaluation process from open
7 meeting laws, which findings focused on the need for "secure
8 documents."

9 The statute is not ambiguous on what remains confidential
10 after the neutral evaluation process is completed. What remains
11 protected are the more specific items listed in Government Code
12 § 53760.3(q): "statements made," "information disclosed," and
13 "documents prepared or produced" or, as listed later in the
14 provision, "communication," "document," and "writing." This is
15 generally consistent with the "secure document" finding of § 7 of
16 AB 506.

17 But the statute is ambiguous about the temporal aspect of
18 the meaning of the phrase "maintain the confidentiality of the
19

20 ⁷The precise finding in AB 506 on this point is:

21 (g) Through the neutral evaluation process, the neutral
22 evaluator, a specially trained, neutral third party, can
23 assist the municipality and its creditors and stakeholders
24 to fully explore alternatives, while allowing the interested
25 parties to exchange information in a confidential
26 environment with the assistance and supervision of a neutral
27 evaluator to determine whether the municipality's
28 contractual and financial obligations can be renegotiated on
a consensual basis.

Cal. Assembly Bill 506, § 1(g), enacted and approved by Governor,
Oct. 9, 2011.

1 neutral evaluation process" in Government Code § 53760.3(q). In
2 context, the court concludes that it is a reference to the entire
3 process that functions to impose a shroud of secrecy only during
4 the pendency of the process. During the pendency of the process,
5 it is not permissible to reveal the number and length of
6 meetings, the identity of the participants, the types of issues
7 discussed, and the status of negotiations because that
8 information is part of the "confidentiality of the neutral
9 evaluation process." While there may be good reason to continue
10 to protect "statements made," "information disclosed," and
11 "documents prepared or produced" even after the neutral
12 evaluation process concludes, the justification is weaker for
13 protecting the number and length of meetings, identity of
14 participants, types of issues discussed, and status of
15 negotiations when the process concludes.

16 This brings into focus the City's request that this court
17 grant permission under the authority conferred on a bankruptcy
18 judge by Government Code § 53760.3(q)(2) to reveal: (1) the
19 number and length of meetings between the City and its various
20 creditors; (2) the identity of the participants at such meetings;
21 (3) the types of issues discussed; and (4) the status of
22 negotiations between the City and each interested party as of the
23 petition date.

24 While this information was appropriately embargoed during
25 the conduct of the neutral evaluation process by virtue of the
26 "maintain the confidentiality" clause, that confidentiality
27 protection ceased, as a matter of California law, once that

1 process ended. Accordingly, there is no present impediment of
2 California law to revelation of that information in and during
3 the chapter 9 case.

4 The remainder of the City's request – to reveal "financial
5 and other information shared, the offers exchanged and the
6 discussions between the parties" – does remain protected by
7 § 53760.3(q) because those categories fit within the statutory
8 categories "statements made, information disclosed, or documents
9 prepared or produced" for which protection unambiguously survives
10 after completion of the neutral evaluation process.

11 This court is not presently persuaded that any of the
12 statements made, information disclosed, or documents prepared or
13 produced during the neutral evaluation process, all of which
14 remain protected under the California confidentiality
15 requirement, are "necessary ... to determine eligibility" under
16 § 109(c)(2). CAL. GOVT. CODE § 53760.3(q)(2). As to eligibility
17 issues under §§ 109(c)(1) and (c)(3), (c)(4), and (c)(5), those
18 are federal issues that will be addressed in the next section.

19 As to the state law issue under § 109(c)(2), the information
20 that either is not, or is no longer, protected (i.e. number and
21 length of meetings, identity of participants, types of issues
22 discussed, and status of negotiations as of petition date) is
23 eligible to be used without restriction and ought to suffice to
24 establish at least a prima facie case that § 109(c)(2) has been
25 satisfied and that, as a matter of California law, the City is
26 permitted to file a chapter 9 case. Indeed, as to status of
27 negotiations, counsel for the City announced during the hearing

1 on the motion that agreements had been reached with two unions to
2 amend collective bargaining agreements.

3 Accordingly, the City's request under California Government
4 Code § 53760.3(q)(1) will be denied, without prejudice to being
5 revisited in the event a subsequent contest over § 109(c)(2)
6 arises.

7
8 C

9 The analysis now shifts to the federal law facet of the
10 confidentiality issue. All chapter 9 eligibility issues except
11 § 109(c)(2) are creatures of federal law, and federal law
12 provides the rule of decision.

13 Federal policy is as encouraging of settlements as is state
14 law, but it takes the different tack of preferring such tools as
15 limiting admissibility in evidence and the protective order as
16 being able to be fashioned to particular situations with more
17 precision than a blanket privilege.

18
19 1

20 We begin by dispensing with the issue of privilege. Federal
21 Rule of Evidence 501 controls privileges in federal litigation
22 and, as relevant to settlement and mediation discussions, relies
23 on federal common law.

24 As no settlement discussion privilege or mediation privilege
25 is recognized in either the U.S. Constitution, or a federal
26 statute, or rules prescribed by the Supreme Court, the question
27 becomes whether there is a common-law privilege that has been

1 judicially recognized "in the light of reason and experience."
2 Fed. R. Evid. 501.

3 There is an ongoing debate over whether there should be a
4 federal common law settlement negotiation privilege. In re MSTG,
5 Inc., 675 F.3d 1337, 1342 (Fed. Cir. 2012) ("MSTG"). The
6 circuits that have addressed the question are divided. The Sixth
7 Circuit recognizes such a privilege; the Seventh Circuit and the
8 Federal Circuit do not. Goodyear Tire & Rubber Co. v. Chiles
9 Power Supply, Inc., 332 F.3d 976, 979-83 (6th Cir. 2003)
10 (privilege recognized); In re Gen. Motors Corp. Engine
11 Interchange Litigation, 594 F.2d 1106, 1124 n.20 (7th Cir. 1979)
12 (no privilege); MSTG, 675 F.3d at 1343-48 (no privilege).
13 Although the Ninth Circuit does not appear to have taken a
14 position, district courts within the Ninth Circuit are divided on
15 the question. Matsushita Elec. Indus. Co. v. Mediatek, Inc.,
16 2007 WL 963975 (N.D. Cal. 2007) (no privilege); California v.
17 Kinder Morgan Energy Partners, L.P., 2010 WL 3988448 (privilege
18 recognized).

19 For purposes of the present situation, this court is
20 persuaded by the Federal Circuit's comprehensive analysis that a
21 settlement negotiation privilege is not necessary. In
22 particular, other tools in the toolbox – especially the
23 protective order – are adequate to protect confidentiality of
24 settlement discussions where necessary to promote settlement.
25 See MSTG, 675 F.3d at 1346-47. Since neither the Ninth Circuit
26 nor the Supreme Court has recognized a settlement negotiation
27 privilege as a matter of federal common law, this court holds

1 that the California neutral evaluation process is not protected
2 by a privilege.

3
4 2

5 The lack of privilege is not the end of the matter. Federal
6 policy favors settlement and disfavors undermining settlement
7 discussions in a manner that could chill the productivity of such
8 discussions in future situations.

9
10 a

11 Federal Rule of Evidence 408 prohibits admission into
12 evidence in civil litigation of compromise offers and statements
13 made in negotiations to prove or disprove the validity or amount
14 of a disputed claim or to impeach by prior inconsistent statement
15 or contradiction. Fed. R. Evid. 408.

16 An objection to the proffer of any evidence in this case of
17 statements made, information disclosed, or documents prepared or
18 produced during the pre-filing neutral evaluation process, either
19 during a hearing or in motion papers and declarations, will have
20 a sympathetic reception in the eyes of the court.

21
22 b

23 A protective order issued under the court's inherent
24 authority is also appropriate to preserve confidentiality in this
25 chapter 9 proceeding of the statements made, information
26 disclosed, or documents prepared or produced during the pre-
27 filing neutral evaluation process.

1 Although those pre-filing discussions concluded, the
2 settlement discussions are not finished. Experience of cases
3 such as Vallejo in this judicial district teaches that fashioning
4 a successful plan of adjustment is more of an exercise in
5 negotiation and compromise than a litigation exercise.

6 Accordingly, a sitting bankruptcy judge from another
7 district has been appointed as Judicial Mediator to be available
8 to serve the needs of this case, without prejudice to the ability
9 of the parties also to employ private persons to facilitate
10 discussions. This measure is consistent with the policy inherent
11 in the alternative dispute resolution provisions in the Federal
12 Judicial Code. 28 U.S.C. §§ 651-53. Confidentiality is
13 expressly contemplated. 28 U.S.C. § 652(d).

14 Whatever goodwill, confidence, and lines of communication
15 that may have been established during the pre-filing neutral
16 evaluation process deserve to be fostered with the certainty that
17 will be useful in the discussions during this case. Such
18 discussions will be vital to the formulation of a successful plan
19 of arrangement.

20 In issuing such a protective order, this court is taking an
21 incremental approach. As the case develops, it may become
22 appropriate to relax the protective order in various respects so
23 that the rights of all parties can be fully examined.

24 As a first increment of disclosure, it is appropriate (and
25 "necessary" if an appellate court were to hold that the
26 California statute applies to all eligibility questions) to
27 authorize the City to release its "790-page 'ask' created by the

1 City that details the City's current situation and lays out a
2 proposed plan – equivalent to a chapter 9 plan – to address the
3 City's financial shortfall."

4 This limited disclosure is necessary in light of the ruling
5 by the Bankruptcy Appellate Panel of the Ninth Circuit in Vallejo
6 that § 109(c)(5)(B), upon which the City relies for eligibility,
7 "requires negotiations with creditors revolving around a proposed
8 plan, at least in concept." Vallejo, 408 B.R. at 297.

9 Disclosure of the proposed plan that formed the basis for
10 discussions during the pre-filing early neutral evaluation is
11 part of the City's prima facie case on the issue of eligibility.

12 As noted, if objections to the petition are made that place
13 various elements of eligibility in actual dispute, then further
14 relaxations of the protective order will be appropriate.

15 16 Conclusion

17 With respect to the question of eligibility under 11 U.S.C.
18 § 109(c)(2), the City's motion will be denied as unnecessary to
19 the extent that it seeks permission to dispense with
20 confidentiality of the California pre-filing neutral evaluation
21 process with respect to the number and length of meetings between
22 the City and its creditors, the identity of the participants at
23 such meetings, the types of issues discussed, and the status of
24 negotiations between the City and each interested party as of the
25 petition date. Those matters are no longer confidential under
26 California law. The remainder of the motion, insofar as it is
27 based on California Government Code § 53760.3(q), is denied,

1 without prejudice.

2 With respect to statements made, information disclosed, or
3 documents prepared or produced during the pre-filing neutral
4 evaluation process, they are not privileged but shall be
5 protected from disclosure by a protective order issued by this
6 court forbidding disclosure, which protective order may be
7 adjusted from time to time. The protective order shall not apply
8 to the "790-page 'ask' created by the City that details the
9 City's current situation and lays out a proposed plan –
10 equivalent to a chapter 9 plan – to address the City's financial
11 shortfall."

12 A separate order will issue.

13 Dated: July 13, 2012.

14
15

UNITED STATES BANKRUPTCY JUDGE
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

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

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:

DEPUTY CLERK