

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF NEW MEXICO

**FILED**  
12:00 MIDNIGHT  
JUN 17 2002

In re:

Furr's Supermarkets Inc.

**DROP BOX**  
United States Bankruptcy Court  
Albuquerque, New Mexico

No. 11-01-10779 SA

Second Amended  
Motion to Compel Payment of Postpetition Taxes out Of the Aggregate Proceeds  
Pursuant to the First Closing Order

Now Comes the New Mexico Taxation and Revenue Department ("Department"),  
states:

1. On September 18, 2002, the Court entered an order, referred to herein as the "First Closing Order,"<sup>1</sup> allowing proceeds to be provisionally paid to the "Lenders" (as that term is used in the "First Closing Order"). Decretal paragraph one provided that "[i]f the Court, at the request of any party in interest should determine that the Lenders for any reason are not entitled to retain any portion of the Aggregate Proceeds paid to the Lenders pursuant to this paragraph 1, the Lenders promptly shall return such portion to the estate as order by the Court in a contested matter."
2. On July 3, 2001, the Court entered an order, referred to herein as the "Fleming Sale Order,"<sup>2</sup> which specifically reserved the right of the

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<sup>1</sup> The Order was actually captioned "First Order Arising Out of Emergency Hearing (1) Authorizing Debtor to Obtain Secured Financing, (2) Granting Adequate Protection and (3) Granting Other Relief, to Permit Short-Term Financing and Use of Cash Collateral."

<sup>2</sup> The Order was captioned "Order (i) Approving Asset Purchase Agreement with Fleming Companies, Inc., (ii) Authorizing the Sale of All or Substantially All of the Debtor's Operating Assets and the Transactions Contemplated by Asset Purchase Agreement, and (iii) Granting Related Relief."

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Department to claim an interest in the sale proceeds on account of its successor in business statutes.

3. At the presentment hearing on July 3, 2001, the Department, through counsel, orally objected to the Fleming Sale Order insofar as it could potentially leave the Department vulnerable with regard to taxes that accrued prior to the sale's closing, but payable subsequent to sale's closing. The Court indicated that the Department should file a separate motion to address that concern.
4. Bankruptcy Code § 552(b)(1) gives the Court broad authority to limit a creditor's prepetition lien on property acquired by the estate postpetition "after notice and hearing and based on the equities of the case." *E.g., In re Ridgeline Structures, Inc.*, 154 B.R. 831 (Bankr. D.N.H. 1993).
5. Both the Final Financing Order,<sup>3</sup> entered March 14, 2001, and the First Closing Order prohibit the Court from modifying the lien priority of the DIP lending (which has been paid), but nothing in any Court order prevents the Court from modifying the priorities of the prepetition lenders according to section 552(b) or otherwise. *See, Final Financing Order* ¶ 21 (any modification of the order cannot affect the priority "with respect to any such DIP indebtedness"); First Closing Order decretal ¶ 6 (same).
6. Title 28 U.S.C. § 960 provides that all "officers and agents conducting any business under authority of a United States court shall be subject to all

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<sup>3</sup> The Order was captioned "Final Order (1) Authorizing Debtor to Obtain Secured Financing, (2) Granting Adequate Protection and (3) Granting Other Relief."

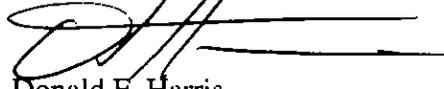
Federal, State and local taxes applicable to such business to the same extent as if it were conducted by an individual or corporation.”

7. Section 960 was enacted in 1934 in response to judicial decisions holding that bankruptcy estates were not required to pay state and local taxes and to prevent debtors from obtaining a competitive advantage against those operating businesses outside of bankruptcy. Act of June 18, 1934, ch. 585, 48 Stat. 993 (1934) (former 28 U.S.C. § 124a); H.R. Rep. No. 1138, 73d Cong. 2d Sess.; *Palmer v. Webster and Atlas Nat'l Bank*, 312 U.S. 156, 166 (1941) (“Its obvious purpose was to negative the idea that a federal receiver or trustee could ignore the rules of law of the state of operation affecting the conduct of the business committed to his charge.”); *Matter of I.J. Knight Realty Corp.*, 501 F.2d 62, 66 (3d Cir. 1974).
8. Section 510(c) has been employed where secured creditors instructed their debtors on which debts to pay or not pay based on the creditor’s self interest. The Department has learned that appeared to have happened here.
9. This congressional concern is apropos to the instant case. If the Lenders’ liens are allowed to attach to the portion of the sale proceeds attributable to postpetition tax collections of the Debtor, the Lenders will have successfully caused (or at least participated in) the Debtor’s pyramiding of tax delinquencies (prepetition and postpetition) for the Lenders’ benefit. The taxpayers would not be subject to that “double whammy” outside of bankruptcy.

10. Title 28 USC § 959(b) requires that a debtor in possession “manage and operate the property in his possession . . . according to the valid laws of the State in which such property is situated . . .” without limitation.
11. The Lenders clearly knew that Furr’s was incurring gross receipts taxes, and in fact desired Furr’s to incur gross receipts taxes (which cannot be avoided if a grocery store operates). Paying taxes in New Mexico is a condition of doing business. *See*, § 7-1-53 NMSA (delinquent taxpayer may be enjoined from doing business in New Mexico).
12. The Department has a statutory lien with respect to all tangible and intangible property of a business, and that interest was preserved with respect to the sale proceeds in the Fleming Sale Order. NMSA § 7-1-61.
13. It would be inequitable for the Lenders’ lien to attach to the sale proceeds to the extent that the Lenders received funds in the blocked accounts that were collected postpetition and attributable to gross receipts taxes under circumstances where the Lenders have refused the debtor the authority to pay those taxes when they came due. The equities of this case compel the result where the Lenders’ collateral would not have been able to have been sold for nearly as much if it were not for Furr’s continued operation postpetition (and necessarily incurring taxes as a result of said operations).
14. Counsel for the Trustee was contacted prior to filing the initial motion, and Trustee’s counsel took no position. Lenders’ counsel was contacted prior to filing the first amended motion and the Lenders opposed the relief requested herein.

WHEREFORE, the Court should order that the Lenders pay to the estate (or to the Department) from the Aggregate Proceeds sufficient funds to pay the postpetition accrued tax, penalty and interest due to the Department.

Respectfully submitted,



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