

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

FILED
12:00 MIDNIGHT
AUG 31 2001

DROP BOX
United States Bankruptcy Court
Albuquerque, New Mexico

In re:

Furr's Supermarkets, Inc.

Debtor

Case No: 11-01-10779 SA

Motion to Convert Case to One Under Chapter 7
And Motion to Limit Notice of Hearing Under Rule 9007 and 2002

Now comes the New Mexico Taxation and Revenue Department ("Department") moving to convert the case to one under Chapter 7, and to limit notice states:

Motion to Convert

1. The Debtor and secured creditors are considering various "wind down budgets" for distributing the remaining assets of the case.
2. On information and belief, the wind down budgets do not seek to provide any funds whatever for any pre-petition creditor who is not a secured creditor.
3. There are possible preference recoveries. There is a \$4 million sum of money which is attributable to a preference settlement.
4. The wind down budget prepared by the Debtor proposed to spend the \$4 million sum, which was set aside for unsecured creditors, for administration of winding down the Debtor. The Department believes

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that all administrative expenses should be born by the secured creditors, under equitable principles or under section 506(c). Although some secured creditors will have a large deficiency, the secured creditors would have lost another \$40 million if it were not for this court.

5. The secured creditors seek to use a “wind down” mechanism as an obvious “end run” around the provisions of section 1129, regarding a liquidating plan, or section 726, regarding distributing property in a Chapter 7 case. The court should not allow such an expansive reading of § 105 of the Code, especially when the unsecured creditor body and the United States Trustee objects.
6. The Debtor and secured creditors are seeking to replace the congressionally legislated provisions with the Debtor’s “business judgment.” There is no support in the bankruptcy code or caselaw for such a breathtakingly expansive notion of the Debtor in Possession’s business judgment.
7. In particular, the Debtor seeks to distribute property to creditors who are not entitled to any statutory priority and to use assets, earmarked *for the estate in the sale order, for expenses relating to preserving the creditor’s collateral*—the collateral being the going concern value of the business which would have been lost were it not for the administrative creditors.

8. The rationale is that the money belongs to the secured creditors, and so long as the secured creditors consent, no other creditor has a right to complain about its application. That is not the law. *Pepper v. Litton*, 308 U.S. 295, 303-04 (1939). *Weinstein v. Park Funding Corp.*, 879 P.2d 462, 465 (Colo. App. 1994); *Goss v. Iverson*, 238 P.2d 1151, 1153 (Idaho 1951).
9. As the Tenth Circuit Court of Appeals noted: "Under established equitable principles, the junior encumbrancer is entitled to have the proceeds of the sale of mortgaged property applied upon the senior indebtedness, whether the property sold was covered by the junior mortgage or not." *Continental Supply v. Marshall*, 152 F.2d 300, 308 (10th Cir. 1945). See also, *In re Penn Central Trans Co.*, 494 F.2d 270 (3rd Cir. 1974); *Republic Financial Group, Ltd. Inc., (South of I-40 v. New Mexico Taxation and Revenue Department and Otero County)*, no. 11-98-02738, Adv. 98-1257 M (October 21, 1999).
10. In this bankruptcy case, the Department is the next in line after administrative claims. Code § 507(a)(8). Indeed, perhaps ahead of administrative claims. NMSA § 7-1-61. The Department may also have a potential administrative claim.

11. The secured creditor, by agreeing with the Debtor to give money to creditors other than the Department and who have a lower priority, may be waiving their liens to that extent under *Continental Supply*.
12. Other provisions of the Code, regarding paying priority creditors less than full, require the priority creditor to consent. Code §§ 1129(a)(9), 1322(a)(2). There is no authority, explicit or implicit under the Code or common law, to circumvent a creditor's statutory priority on the basis of a secured creditor's discretion or a debtor's business judgment.
13. The Department's priority position is established under the Code, and under state law. *Regents of N.M. College of Agric. & Mechanic Arts v. Academy of Aviation, Inc.*, 83 N.M. 86. 488 P.2d 343 (1971).
14. Despite the Department's priority position, the Department has been in negotiations with the unsecured creditors' committee to reach a sharing agreement with an eventual unsecured fund, so that other prepetition, unsecured creditors could receive some dividend, and so that the committee would have an incentive to recover assets—for the benefit of other unsecured creditors and for the Department.
15. On information and belief there has been no meaningful offer to the

unsecured creditor body (priority or general unsecured) for any funds to pay any creditor other than the secured lenders, or creditors who the Debtor is preferring based on its business judgment.

16. In light of the Department's nearly \$4 million priority claim, and the nearly \$100 million in general unsecured claims, the Court should not allow the Debtor and a secured lender to distribute nearly \$100 million, potentially in violation of the Bankruptcy Code and various creditors' rights, based on the Debtor's business judgment. Distribution should be according the Bankruptcy Code.
17. Grounds exists under § 1112(b) for conversion.
18. Both the debtor and the lenders have continually threatened to convert the case to Chapter 7. On that basis, the Department does not believe that there will be grounds to object.

Motion to Limit Notice

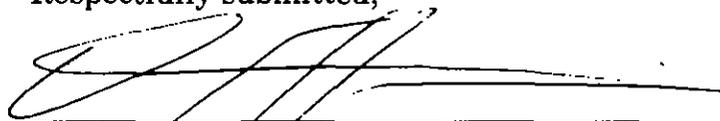
19. On information and belief, the United States Trustee might be filing its own motion to convert shortly or joining the Department's motion. The unsecured creditors' committee and the U.S. Trustee cannot oppose or support this motion at this time. However, the Department, the U.S. Trustee and the committee have had some preliminary discussions regarding potential Chapter 7 Trustees.
20. The Court has authority to regulate notice. Rules 9007, 2002(l) and 2002(m).
21. A hearing on this motion, a possible United States Trustee's motion, and the possible support of those motions by the Unsecured Creditor's

Committee should be scheduled with the continued hearing on the wind down motions on October 4 and 5, 2001.

22. The court should order a reduced mailing list for the hearing or allow the notice to be by publication.
23. Concurrence with the above motions is not necessary under Local Rule 9013.

WHEREFORE, the case should be converted and the court should limit notice of the hearing and consolidate the hearing with the ones coming up on October 4 and 5, 2001.

Respectfully submitted,



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I certify a copy of the foregoing was mailed and faxed this 31st day of August, 2001 to:

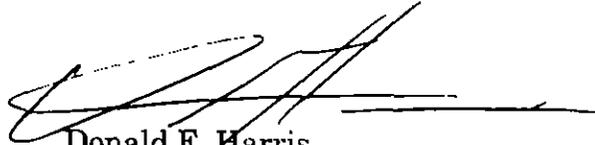
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