

ORIGINAL

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW MEXICO**

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In re §
FURR'S SUPERMARKETS, INC. §
Debtor. §

U.S. BANKRUPTCY COURT
BUENOS AIRES, N.M.
Case No. 11-01-1070
Chapter 11

**MOTION OF LSF BASSETT, L.P. TO
COMPEL DEBTOR TO PAY POST-PETITION OBLIGATIONS
UNDER UNEXPIRED LEASE OF NONRESIDENTIAL REAL PROPERTY**

LSF Bassett, L.P., a creditor and party-in-interest in the above-styled and numbered bankruptcy case, hereby files this its "Motion to Compel Debtor to Pay Post-Petition Obligations Under Unexpired Lease of Nonresidential Real Property", pursuant to 11 U.S.C. §§ 365(d)(3) and 503(b)(1), as follows.

I.

PARTIES, JURISDICTION AND VENUE

1. Movant LSF Bassett, L.P. ("Bassett") is a creditor and party-in-interest in the above-styled and numbered bankruptcy case.
2. This Court has jurisdiction of this contested matter pursuant to 28 U.S.C. § 1334. This is a "core" proceeding pursuant to 28 U.S.C. § 157(b)(2)(B).
3. Venue is proper in this Court pursuant to 28 U.S.C. § 1409.

II.

BACKGROUND

A. Procedural Posture of Case.

4. Furr's Supermarkets, Inc. ("Debtor") filed its voluntary petition for relief under Chapter 11 of Title 11 of the United States Code on February 8, 2001. Debtor continues in possession of its property and operation of its business as a debtor-in-possession pursuant to 11 U.S.C. §§ 1107 and 1108.
5. Debtor filed its "Motion for Order Extending Time Within Which Debtor May Assume or Reject Unexpired Leases of Nonresidential Real Property" on or about March 1, 2001 seeking an extension

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of time to assume or reject a number of unexpired leases of nonresidential real property, including the Lease. This Court signed and entered an order granting such extension over the objection of Bassett and others on April 6, 2001, and extended the deadline under 11 U.S.C. § 365(d)(4) by which Debtor must assume or reject unexpired nonresidential leases until August 10, 2001.

B. Debtor's Lease With Bassett.

6. Bassett is the lessor under an unexpired lease of non-residential real property (the "Lease") known as Furr's Lease No. 370, located in the Bassett Shopping Center, 1117 Geronimo, El Paso, Texas (the "Center"). The premises covered by the Lease (the "Premises") are used by the Debtor in the operation of a grocery store. A true and correct copy of the Lease is attached hereto as Exhibit "1" and incorporated herein by reference.

7. Pursuant to the Lease, the Debtor is obligated to pay on a monthly basis a total of \$32,289.00, comprised of the following:

Base Monthly Rent	\$28,683.00
CAM charges	\$2,132.00
Marketing costs	<u>\$1,474.00</u>
Total Monthly	\$32,289.00

8. In addition, the Lease obligates the Debtor to pay semi-annually bonus rental payments determined on the basis of the amount by which the Debtor's gross sales during the period multiplied by a factor of 1.25% exceed the Monthly Rent payable for such lease year. However, the threshold level of sales to trigger the bonus rentals has not, to the best information and belief of Bassett, ever been reached.

9. Finally, and most importantly for purposes of this motion, the Lease obligates the Debtor to pay in arrears on an annual basis the property taxes assessed against the Premises.¹ The Lease requires

¹ Section 10 of the Lease provides: "Real Property Taxes. Lessor agrees to pay all real estate taxes and assessments levied upon and assessed against the Center except for those real estate taxes and assessments levied upon and assessed against the Premises and the Parking Area depicted on Exhibit "D". Further, to facilitate Lessee's payment of the real estate taxes hereinafter agreed to be paid by Lessee, Lessor agrees to obtain separate tax bills for the Premises and the Parking Area depicted on Exhibit "D". Lessee shall pay and discharge, in addition to the rent herein reserved, all real estate taxes and assessments levied upon and assessed against the Premises and the Parking Area depicted on Exhibit "D" and the improvements to be constructed thereon in accordance with the Plans and Specifications for any period, all of which is included within the term of this Lease, and also its pro rata share of all taxes and assessments levied or assessed thereon for any period, part of which is included within the term of this Lease. In addition, Lessee shall

the Debtor to pay and discharge in addition to rent all taxes assessed against the Premises for any period all of which is included in the term of the Lease, or its pro rata share of any such taxes for any period part of which is included in the term of the Lease.

10. While not expressly set forth in the Lease, Bassett's normal custom and practice has been to pay the taxes on the Premises prior to the February 1 delinquency date, and invoice the Debtor for the taxes. Typically, these invoices have been mailed to the Debtor between February and April of each year, with payment of said invoices due within thirty (30) days after the invoice is mailed.

11. The taxes assessed against the Premises for the year 2000 by the El Paso City Tax Collector/Assessor were in the amount of \$41,088.75. Bassett received the tax bill in the normal course and paid it prior to February 1, 2001. On or about January 19, 2001, Bassett sent to the Debtor an invoice for the 200 taxes in the amount of \$41,088.75. Said invoice remains unpaid. A true and correct copy of said invoice is attached hereto as Exhibit "2" and incorporated herein by reference.

12. Taxes for the year 2001 have been accruing since January 1, 2001, although the precise amount of said taxes will not be determined until October 2001 and not payable to the taxing authorities until February 1, 2002.

13. To date, the Debtor has not moved to either assume or reject the Lease.

14. To date, the Debtor has remained substantially current in payment of the post-petition monthly rentals, but has not paid any part of either the 2000 taxes or made any provision for payment of the 2001 taxes.

pay and discharge, in addition to the rent herein reserved, all personal property taxes levied or assessed against personal property in or about the Leased Premises for any period all of which is included within the term, and also its pro rata share of all such taxes and assessments levied or assessed thereon for any period, part of which is included within the term. Nothing contained in this Lease shall be deemed or construed to require Lessee to pay or discharge any tax which may be levied upon the income, profits or business of Lessor or any personal property taxes, franchise, inheritance or state taxes or taxes upon inheritance or right of succession which may be levied against any estate or interest of Lessor even though such taxes may become a lien against the Premises."

III.

GROUNDS FOR COMPELLING PAYMENT OF TAXES

A. Texas Property Tax Code.

The statutory scheme for taxation of real property in the State of Texas is set forth in Title 1 of the Texas Tax Code². Real property is taxable by a taxing unit if located in the unit on January 1.³ On January 1 of each year, a tax lien attaches to property to secure the payment of all taxes, penalties, and interest ultimately imposed for the tax year on such property.⁴ Property taxes are the personal obligation of the person who owns or acquires the property on January 1 of the year for which the tax is imposed.⁵

By July 25, the chief appraiser is to prepare and certify the appraisal roll listing the property taxable by the taxing unit.⁶ Before the later of September 30 or the 60th day after the date the certified appraisal roll is received by the taxing unit, the taxing unit is to adopt a tax rate for the current tax year and notify the assessor for the unit of the rate adopted.⁷ On receipt of notice of the tax rate for the current tax year, the assessor for a taxing unit other than a county is to calculate the tax imposed on each property included on the appraisal roll for the unit.⁸ The appraisal roll with amounts of tax entered as approved by the governing body constitutes the unit's tax roll.

² V.T.C.A., Tax Code § 1.01 et seq.

³ V.T.C.A., Tax Code § 21.01.

⁴ V.T.C.A., Tax Code § 32.01.

⁵ V.T.C.A., Tax Code § 32.07.

⁶ V.T.C.A., Tax Code § 26.01.

⁷ V.T.C.A., Tax Code § 26.05.

⁸ V.T.C.A., Tax Code § 26.09.

The assessor for each taxing unit then is to prepare and mail a tax bill to each person in whose name the property is listed on the tax roll by October 1 or as soon thereafter as practicable.⁹ Taxes are due on receipt of the tax bill and are delinquent if not paid before February 1 of the year following the year in which imposed.¹⁰

B. 11 U.S.C. § 365(d)(3).

1. *Background of Section 365(d)(3).*

Section 365(d)(3) of the Bankruptcy Code requires the trustee or debtor-in-possession to timely perform all the obligations of the debtor, except those specified in section 365(b)(2), arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected.¹¹ 11 U.S.C. § 365(d) provides:

"(3) The trustee shall timely perform all the obligations of the debtor, except those specified in section 365(b)(2), arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected, notwithstanding section 503(b)(1) of this title. The court may extend, for cause, the time for performance of any such obligation that arises within 60 days after the date of the order for relief, but the time for performance shall not be extended beyond such 60-day period. This subsection shall not be deemed to affect the trustee's obligations under the provisions of subsection (b) or (f) of this section. Acceptance of any such performance does not constitute waiver or relinquishment of the lessor's rights under such lease or under this title."

Prior to the 1984 enactment of § 365(d)(3), the payment of post-petition lease obligations prior to assumption or rejection of an unexpired lease was governed by the administrative expense provisions of 11 U.S.C. § 503(b)(1). Under that subsection, bankruptcy courts ordinarily allowed as an administrative expense the amount of the rent the court found to be reasonable, and prorated that rent over the post-petition, pre-rejection period.¹² Furthermore, when the lease required the debtor-tenant to reimburse the landlord for

⁹ V.T.C.A., Tax Code § 31.01.

¹⁰ V.T.C.A., Tax Code § 31.02.

¹¹ 11 U.S.C. § 365(d)(3).

¹² *In re McCrory Corp.*, 210 B.R. 934, 936 (S.D.N.Y. 1997).

real estate taxes. the courts only allowed as an administrative expense a prorated payment of real estate taxes over the post-petition, pre-rejection period, regardless of the billing date.¹³

The enactment of Section 365(d)(3) eliminated the bankruptcy court's discretion to alter the amount of the rent and other charges to be paid under a lease of non-residential real property.¹⁴ Instead, 11 U.S.C. § 365(d)(3) requires the trustee or debtor-in-possession to provide landlords of non-residential real property full and timely payment for services due under an unexpired lease during the post-petition, pre-rejection period. While the legislative history of the amendment is rather sparse, Senator Orrin Hatch's comments are indicative of the concerns Congress attempted to address by the amendments:

"A second and related problem is that during the time the debtor has vacated space but has not yet decided whether to assume or reject the lease, the trustee has stopped making payments due under the lease. These payments include rent due the landlord and common area charges which are paid by all the tenants according to the amount of space they lease. In this situation, the landlord is forced to provide current services--the use of its property, utilities, security, and other services--without current payment. No other creditor is put in this position. In addition, the other tenants often must increase their common area charge payments to compensate for the trustee's failure to make the required payments for the debtor. This bill would lessen these problems by requiring the trustee to perform all the obligations of the debtor under a lease of nonresidential real property at the time required in the lease. This timely performance requirement will insure that debtor-tenants pay their rent, common area, and other charges on time pending the trustee's assumption or rejection of the lease."¹⁵

Since the 1984 amendments, the debtor's obligation to pay in full all rent which accrues on a monthly basis after the petition date and prior to the date of rejection under an unexpired lease of non-residential real property has been clearly settled.¹⁶ A question which has, however, been less than settled involves the treatment of ad valorem taxes assessed against the property and which the debtor is obligated under its lease to pay or reimburse its landlord. This is particularly so in situations where, as here, the prior year's taxes

¹³ *Id.*, citing *Matter of J. Bam, Inc.*, 554 F.2d 255 (5th Cir.1977).

¹⁴ *Id.*, citing 3 *Collier on Bankruptcy*, § 503.04 at 527.

¹⁵ H.R. Conf. Rep. No. 882, 98th Cong., reprinted in 1984 U.S. Code Cong. & Admin. News 576, quoted in *In re Child World, Inc.*, 161 B.R. 571, 575 n. 6 (S.D.N.Y. 1993).

¹⁶ See e.g. *In re Pudgie's Dev. of N.Y.*, 223 B.R. 421, 426 (Bankr.S.D.N.Y. 1998).

were paid in arrears and invoiced to the debtor by the landlord for a period prior to commencement of the case. Such circumstances raise an important question of the proper construction, as it relates to taxes, of the requirement under Section 365(d)(3) that the debtor timely perform all post-petition obligations of the debtor under an unassumed non-residential lease. Specifically, does Section 365(d)(3) obligate the debtor to pay or reimburse taxes *that become due* during the post-petition, pre-rejection period, or does Section 365(d)(3) require the debtor to pay only the taxes *that accrue* during the post-petition, pre-rejection period?

2. *Competing Approaches to Tax Question.*

Neither the United States Supreme Court nor the Tenth Circuit Court of Appeals have expressly decided the question of the proper treatment of taxes payable under a non-residential lease of the debtor during the post-petition, pre-rejection period issue. Other courts which have addressed the issue have been split, although the Seventh Circuit Court of Appeals has adopted the pro-ration approach followed by a majority of courts rather than the billing approach followed by the minority.¹⁷

The majority approach holds that, although the language of 11 U.S.C. § 365(d)(3) is ambiguous, when viewed in light of its context in the Bankruptcy Code and its legislative history, it requires payment of only those taxes that accrued after entry of the order for relief.¹⁸ The majority position is consistent with the long-standing, pre-1984 practice of prorating payment of a debtor's obligations under a lease, regardless of the billing date.¹⁹ The majority approach requires payment under 11 U.S.C. § 365(d)(3) of those but only those taxes that can be said to have "accrued" during the pre-rejection period, regardless of the billing date.²⁰

¹⁷ *Matter of Handy Andy Home Improvement Centers, Inc.*, 144 F.3d 1125 (7th Cir. 1998), *affirming National Terminals Corp. v. Handy Andy Home Imp. Centers, Inc.*, 222 B.R. 149 (N.D.Ill. 1997).

¹⁸ *In re Learningsmith, Inc.*, 253 B.R. 131, 133 (Bankr.D.Mass. 2000).

¹⁹ *In re McCrory Corp.*, 210 B.R. 934, 937 (S.D.N.Y. 1997).

²⁰ Cases adopting the majority approach include *Matter of Handy Andy Home Improvement Centers, Inc.*, *supra*; *In re McCrory Corp.*, *supra*; *In re All for A Dollar, Inc.*, 174 B.R. 358 (Bankr.D.Mass.1994); *In re Schneider, Inc.*, 175 B.R. 769 (S.D.Ia.1994); *In re Almac's, Inc.*, 167 B.R. 4 (Bankr.D.R.I.1994); and *In re Child World, Inc.*, 161 B.R. 571 (S.D.N.Y.1993).

The minority approach, in contrast, holds that the language of 11 U.S.C. § 365(d)(3) unambiguously requires payment in full of the amount of taxes that became due after entry of the order for relief without regard to when it accrued.²¹ These cases hold that a debtor who is a tenant under a nonresidential real property lease must pay in full all bills received from the landlord during the post-petition, pre-rejection period, regardless of when those charges accrued.²²

The Seventh Circuit Court of Appeals in *Matter of Handy Andy Home Improvement Centers, Inc.*, is the only Court of Appeals to have addressed this question. In that case, the Seventh Circuit endorsed the pro-ration approach accepted by a majority of the lower courts which have considered the issue. The Court whole-heartedly rejected the minority view as "neither inevitable nor sensible". The Court criticized the *billing-date approach*, which requires payment in full of tax obligations which become due after the entry of the order for relief without regard to when they accrued, because it "would make the rights of creditors turn on the happenstance of the dating of tax bills and the strategic moves of landlords and tenants."²³ The Court instead adopted the pro-ration approach and affirmed the decision of the District Court, holding that the debtor was obligated under Section 365(d)(3) to pay the landlord real estate taxes which accrued from the date of the entry of the order for relief through the date of rejection of the lease.²⁴ In so doing, the Court made it clear that the pro-ration approach requires pro-ration of the taxes on a daily basis:

"The taxes had been paid, by National. Handy Andy wasn't trying to borrow money from National. What it wanted was the continued occupancy of the leased property until it rejected the lease. To get this benefit it had to pay the full rent under the lease for every day that it continued to occupy the property; section 365(d)(3) ... requires no less."

²¹ *In re Learningsmith, Inc.*, *supra*.

²² Cases adopting the minority view include *In Re DeCicco of Montvale, Inc.*, 239 B.R. 475, 478-483 (Bankr.D.N.J.1999); *In Re Krystal Co.*, 194 B.R. 161 (Bankr.E.D.Tenn.1996); and *In Re R.H. Macy & Co., Inc.*, 152 B.R. 869 (Bankr.S.D.N.Y.1993).

²³ *Matter of Handy Andy Home Improvement Centers, Inc.*, *supra* at 1128.

²⁴ *In Re Handy Andy Home Imp. Centers, Inc.*, 196 B.R. 87, 96 (Bankr.N.D.Ill. 1996).

C. Request for Payment of Taxes.

The majority approach, which requires payment by the debtor of post-petition, pre-rejection taxes as they accrue, appears to be the better approach. Under the minority approach, the Debtor could (with respect to its leases in Texas) avoid payment of taxes altogether by simply timing its filing just after February 1, after receipt from its landlords but before payment of invoices for its share of the 2000 property taxes. Under the minority approach, not only would the Debtor avoid payment of the 2000 taxes, whose billing date was just prior to commencement of the case, but the Debtor would also avoid payment of the current year taxes, even those accruing during the post-petition, pre-rejection period. This result would attain because, in all likelihood, the decision to assume or reject the lease would be made by the Debtor long before February 1, 2002, the billing date for the current taxes. The minority approach would give the Debtor what Section 365(d)(3) was designed to avoid: the Debtor would get current services in the form of continued occupancy of the Premises without making current payments, at least of the taxes attributable to Premises during the period of its post-petition occupancy.

The majority approach is the better approach because it obligates the Debtor to make payment of current taxes as they accrue without regard to the billing date. The majority approach is consistent with the policies behind Section 1 U.S.C. § 365(d)(3) and is the approach that should be adopted by this Court.

The Texas property tax scheme, under which property taxes are not billed until October of the year in which they accrue and are not due until February 1 of the following year, presents practical but not insurmountable problems with respect to fashioning an order to insure that the Debtor complies with its obligations under 11 U.S.C. § 365(d)(3). Taxes are accruing against the Premises, although the precise amount of the taxes will not be determined until October, 2001. Nevertheless, absent some compelling circumstances which materially affect the valuation of the property being taxed, real property taxes do not vary substantially from year to year. Seldom do they go down. The Debtor should be obligated to pay on a monthly basis 1/12 of the current year's taxes on the Premises, estimated on the basis of the 2000 taxes,

subject to adjustment upon the receipt by Bassett of the current year's tax bill. Such payments of \$3,424.06 should be made along with rent and other charges under the Lease on a monthly basis until the Debtor assumes or rejects the Lease. Naturally, the taxes which have accrued from February 8, 2001 through the date of entry of the order on this motion should be paid to Bassett in full immediately. This approach represents a satisfactory and practical solution to the mandates of 11 U.S.C. § 365(d)(3) as it has been interpreted by a majority of the Courts.

WHEREFORE, LSF Bassett, L.P. requests that this Court enter an order requiring Debtor to: (1) immediately pay to Bassett for real property taxes accrued under the Lease from February 8, 2001 to the date of entry of such order at the rate of \$3,424.06 per month; (2) pay to Bassett for real property taxes the sum of \$3,424.06 on the first (1st) day of each month from and after the date of entry of the order until assumption or rejection of the Lease by the Debtor; and (3) pay to Bassett its reasonable attorneys fees and

costs incurred in obtaining such order; and enter such other and further orders as are just.

DATED: May 24, 2001.

Respectfully submitted,

BUSH CRADDOCK & RENEKER, L.L.P.

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