

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF NEW MEXICO

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U.S. BANKRUPTCY COURT  
ALBUQUERQUE, NM

In re:

FURR'S SUPERMARKETS, INC.,

Case No. 11-01-10779-SA  
Chapter 11

Debtor.

**DEBTOR'S MOTION TO REJECT SUBLEASE WITH PINNACLE LOGISTICS,  
INC. AND FOR AN ORDER DECLARING THAT THE DEBTOR'S  
LEASEHOLD RIGHTS IN THE EL PASO DISTRIBUTION CENTER ARE FREE  
AND CLEAR OF ANY CLAIMS OF PINNACLE LOGISTICS, INC.**

Furr's Supermarkets, Inc., debtor-in-possession (the "Debtor"), asks that the Court (i) allow the Debtor to reject a certain sublease between the Debtor and Pinnacle Logistic, Inc. ("Pinnacle"), and (ii) enter an order declaring that the Debtor's rights in the leasehold of the El Paso Distribution Center are free of any rights asserted by Pinnacle pursuant to the sublease or otherwise, and in support hereof states:

1. On February 8, 2001 (the "Petition Date"), the Debtor filed with this Court its voluntary petition for relief under chapter 11 of the Bankruptcy Code. The Debtor continues to operate its businesses and manage its properties as debtor-in-possession pursuant to sections 1107 and 1108 of the Bankruptcy Code.

2. The Debtor is the lessee under a long-term lease (the "Lease") of certain improved real estate in El Paso, Texas, with a street address of 9820 Railroad Drive and 9601

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Railroad Drive, which the Debtor uses or has used as its main warehouse for storing and distributing food, produce, and other goods to its grocery stores (the "Distribution Center").

3. Under the Lease, the Debtor pays rent of approximately \$66,000 per quarter.

4. On September 23, 1998, the Debtor and Pinnacle entered into a certain Warehousing and Distribution Agreement (the "Management Agreement"), pursuant to which Pinnacle agreed to operate the Distribution Center for the Debtor, in exchange for repayment of all costs incurred in doing so, together with a management fee of \$1,120,000 per year.

5. Pursuant to the Management Agreement, the Debtor executed a sublease of the Distribution Center to Pinnacle. A true and correct copy of the sublease is attached hereto as Exhibit A (the "Sublease").

6. Under the Sublease, Pinnacle pays rent of \$100 per month to the Debtor, which is less than one half of one percent of the rent the Debtor pays to the landlord.

7. The Debtor has filed a motion to reject the Management Agreement, and has stopped using the Distribution Center and Pinnacle's services under the Management Agreement.

8. The Debtor estimates that the value of its leasehold interest in the Distribution Center is several million dollars.

9. Pinnacle asserts that, pursuant to 11 U.S.C. §365(h), it will continue to have a subleasehold interest in the Distribution Center even after the Management Agreement and the Sublease have been rejected. Pinnacle makes this assertion despite that fact that, inter

alia, (i) the Sublease rent is only a token amount; (ii) the Sublease terminates when the Management Agreement terminates; (iii) Pinnacle cannot assign or sublet the Sublease without the Debtor's consent; (iv) Pinnacle may only use the Distribution Center pursuant to the terms and conditions of the Management Agreement which, upon or before rejection of the Management Agreement, means that Pinnacle has no right to use the Distribution Center, and (v) as described in paragraph 10, Pinnacle's rights under the Sublease will terminate in any event, regardless of §365(h).

10. If Pinnacle were to prevail, the Debtor would be forced to reject its lease of the Distribution Center to avoid future liability under the Lease. Upon rejection of the Lease, Pinnacle would lose any rights under the Sublease and the Debtor's creditors would lose the substantial leasehold value.

11. Even if the Debtor assumed the Lease, Pinnacle could not use the Distribution Center for any purpose other than "operating a food distribution warehouse pursuant to the terms and conditions of the Agreement."

12. Pinnacle's position cannot benefit Pinnacle, only harm the Debtor's creditors. Such a "dog in the manger" position should not be allowed to prevail, especially since Pinnacle appears to be taking the position to obtain a tactical advantage in the bankruptcy case.

13. 11 U.S.C. §365(h) protects the interests of tenants under "true" or "bona fide" real property leases. See In re Lunan Family Restaurants, 194 B.R. 429, 450 (the lease at issue was not entitled to the protections of §365(h) because it was not a "true lease,"

determined using the “economic substance” test). Cf. In re Dune Hotel Associates, 212 B.R. 110 (Bankr. D. S.C. 1997) (§365(h) protections were available to a lease, overruling the debtor’s argument that the transaction was not really a lease) See generally International Trade Administration v. Rensselaer Polytechnic Institute, 936 F.2d 744 (2d Cir. 1991) (§365(d)(4) applies only to “true” or “bona fide” leases, and courts may look to the economic substance of a transaction to determine whether a denoted “lease” is really a sale or other arrangement); In re PCH Associates, 804 F.2d 193 (2d Cir. 1986) (to the same effect); In re Moreggia & Sons, Inc., 852 F.2d 1179 (9th Cir. 1988) (to the same effect).

14. The Sublease is not a “true” or “bona fide” lease, but is instead an integral part of the Management Agreement that conveys no independent real property rights to Pinnacle. The “economic substance” of the transaction between the Debtor and Pinnacle was for Pinnacle to manage and operate the Distribution Center, not to sublease the Distribution Center. Pinnacle was given the Sublease to insure that Pinnacle’s occupancy of the Distribution Center did not constitute a breach of the Lease. That is why the Sublease rent is only \$100 per month. See In re Lunan Family Restaurants, 194 B.R. at 451 (the lease at issue was not a bona fide lease because, inter alia, it required payments of \$1 per year). The parties never intended for Pinnacle to have any rights to the Distribution Center after they ceased to operate under the Management Agreement, or to have any interest in the Distribution Center other than as governed by the Management Agreement.

15. The lack of independent value and significance of the Sublease is shown in part by the fact that, to the Debtor’s knowledge, Pinnacle never executed the Sublease. The

Sublease copy attached hereto was supplied to the Debtor by Pinnacle, and it is not signed by Pinnacle. Thus, when the Debtor filed its bankruptcy case the Sublease was not effective. For this reason also, Pinnacle has and will have no rights under the Sublease once the *Sublease and Management Agreement have been rejected*.

16. §365(h) provides that the lessee's rights are protected upon rejection of the lease by the lessor only to the extent "that such rights are enforceable under applicable nonbankruptcy law." Under the applicable state law, Pinnacle will have no real property interest in, or even any right to use, the Distribution Center once Pinnacle ceases operating the Distribution Center for the Debtor. Accordingly, Pinnacle has no rights that are protected by §365(h).

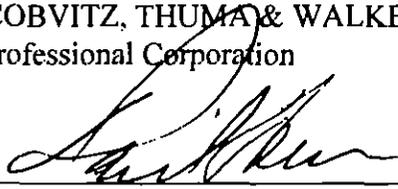
17. While rejection of an executory contract ordinarily is not tantamount to termination of the contract, in the particular circumstances of this case the Court should rule that the Debtor's combined rejection of the Management Agreement and the Sublease have the effect of terminating all of Pinnacle's rights under the Sublease.

18. Pinnacle opposes the relief requested by this Motion.

WHEREFORE, the Debtor requests that the Court (i) allow the Debtor to reject the Sublease, (ii) enter an order declaring that upon the rejection of the Management Agreement

and the Sublease, Pinnacle shall have no rights of any kind in the Debtor's leasehold interest in the Distribution Center; and (iii) for all other just and proper relief.

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This certifies that on July 30, 2001,  
a copy of this Motion was mailed by  
First Class United States mail to:

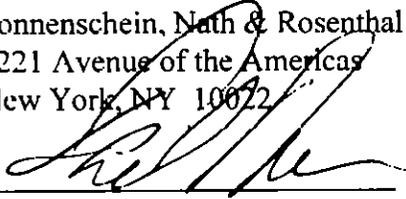
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*11/2/2004  
Jm 1/23/04*

**SUBLEASE**

This Sublease (the "Sublease") is entered into as of the 10th day of October, 1998, by and between Furr's Supermarkets, Inc., a Delaware corporation ("FSI"), and Pinnacle Logistics, Inc., a Delaware corporation ("Pinnacle").

**RECITALS**

A. Effective October 19, 1998, FSI and Pinnacle entered into a certain Warehousing and Distribution Agreement (the "Agreement"), pursuant to which Pinnacle agreed to operate (or FSI a certain food distribution center in El Paso, Texas (the "Food Distribution Center").

B. Part of the Food Distribution Center consists of the leased real property described in this Sublease, which property is more particularly described in Exhibit A hereto (the "Premises").

C. As of October 19, 1998, FSI holds a leasehold interest in the Premises, pursuant to the terms of a certain lease agreement described on Exhibit A hereto (the "Lease").

D. Pursuant to the terms of the Agreement, FSI agreed to sublease to Pinnacle FSI's leasehold interest in the Premises.

NOW THEREFORE in consideration of the premises and the mutual covenants contained herein, FSI and Pinnacle agree as follows:

1. **Premises: Use.** FSI hereby subleases the Premises to Pinnacle. Pinnacle shall use the Premises for operating a food distribution warehouse pursuant to the terms and conditions of the Agreement.

2. **Term.** The term of this Sublease shall commence on the date hereof and terminate on the earlier to occur of: (i) the date the Agreement terminates; (ii) the date FSI's leasehold interest in the Premises terminates; or (iii) the date this Sublease is terminated pursuant to paragraph 10 below.

3. **Compliance with Lease.** Pinnacle shall comply in all respects with the Lease, the same as if Pinnacle was the lessee under the Lease. Pinnacle acknowledges that it has received a copy of the Lease.

4. **Rent.** Pinnacle shall pay FSI rent in equal monthly installments of \$100 in advance on the 1st day of each month. If the monthly rent is not paid on or before the fifth day of any month, Pinnacle shall pay FSI a late charge of \$5.00. The first month's rent shall be prorated.

5. **Utilities; Taxes; Other Charges.** Pinnacle shall pay (i) all charges for gas, electricity, telephone and all other utility services used in connection with the Premises; (ii) all real property taxes; and (iii) all other amounts to be paid under the Lease. Reimbursement of all such amounts shall be handled pursuant to the terms of the Agreement.

6. **Alterations and Improvements.** Pinnacle shall not make any alterations, additions, improvements, or changes in the Premises without the prior written consent of FSI, which FSI may withhold in its sole discretion.

*Pass disclosure - max is immaterial*

*AS*

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**EXHIBIT**

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