

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

FILED
12:00 MIDNIGHT
SEP 14 2001
LRJP BOX
United States Bankruptcy Court
Albuquerque, New Mexico

In re:

Furr's Supermarkets, Inc.

Case No: 11-01-10779 SA

Objection to Any Cash Collateral or Similar Motion
Permitting Debtor and Secured Creditor to Avoid Paying
State of New Mexico Post-Petition Gross Receipts Tax

Now Comes the New Mexico Taxation and Revenue Department ("Department"),
by and through its undersigned counsel, states:

1. Furr's probably accrued approximately \$1.5 million in gross receipts taxes during the month of August, based on recent months' reporting. Although the gross receipts tax is not a trust fund tax, the fact remains that Furr's and most other retail businesses in New Mexico treat the tax as an "add on" which is charged to the customers and separately stated on the cash register receipts.
2. If the court does not require that the post-petition taxes to be paid, the secured lenders—who were able to prevent tens of millions of additional losses through the use of this court—will have successfully caused the economic transfer of approximately \$1.5 million from the taxpayers of New Mexico to out of state financial institutions.
3. If the Furr's stores had gone dark in February, the taxpayers would have been out approximately \$4 million (but no more), relating to one and one-half months gross receipts tax and an audit liability of approximately \$1.4 million.

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4. If the post-petition taxes are not paid, the taxpayers could be out as much as \$5.5 million.
5. The added \$1.5 million will be a direct loss of revenue caused by this bankruptcy proceeding, and inuring to the benefit of out-of-state financial institutions or others. Consumers in New Mexico would have bought groceries whether or not Furr's was in business in August.
6. Tax collectors have never been popular.¹ Notwithstanding that the tax-collector itself is unpopular, the governmental programs funded by taxes tend to be both necessary and popular. Approximately half of the state budget is devoted to education and most of the budget is funded by the gross receipts tax. Stated differently, \$1.5 million pays for a lot of educational expense and other needed government expenditures.
7. Title 28 U.S.C. § 960 provides that debtors in possession are fully subject to state tax laws. In the bankruptcy context, 28 U.S.C. § 960 indicates "a Congressional purpose to facilitate—not to obstruct—enforcement of state laws." *California Bd. of Equalization v. Sierra Summit*, 490 U.S. 844, 852-53 (1989).
8. The Court's reference to 28 U.S.C. § 960, *Sierra Summit*, highlights a congressional bankruptcy tax policy. Section 960 was enacted to prevent debtors from obtaining a competitive advantage against those operating businesses outside of bankruptcy. *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).

9. “Equality of distribution among creditors is a central policy of the Bankruptcy Code. According to that policy, creditors of equal priority should receive equal shares of the debtor’s property.” *Beiger v. IRS*, 496 U.S. 53, 58 (1990). *See also, Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 161 (1946) (“A purpose of bankruptcy is to administer an estate as to bring about a ratable distribution of assets among the bankrupt’s creditors.”); Code § 726(b) (distribution pro rata when assets insufficient to pay any class of a particular priority).
10. The record will reflect that the Debtor and the lending institutions have authorized payment of all other ordinary course of business expenses, including all federal taxes—trust fund and non-trust fund taxes. There is no basis in the Code or in equity for such discrimination.
11. The Debtor has informed (or implied) the Department that it is the lending institutions that have instructed the Debtor *not* to pay the state taxes for the month of August. Assuming that is an accurate representation, the court should not permit this behavior. *See, In re American Lumber Co.*, 5 B.R. 470 (D.Minn.1980) (court equitably subordinated claim of lender that only allowed its debtor to pay creditors who would directly enhance value of collateral where lender refused to allow its

¹ *See, e.g., 2 Chronicles 10:1-17* (tax increase divided the kingdom in the Old Testament); *Mathew*

debtor to pay sales taxes); *In re Clark Pipe & Supply Co.*, 870 F.2d 1022 (5th Cir. 1989) (same).

12. It would serve no purpose to allow the lenders to avoid paying the post-petition tax claim now only to have their claims, or other insider claims, equitably subordinated under Code § 510(c) later. Whether a lien was granted by a court order is not conclusive of the equitable subordination issue. *Pepper v. Litton*, 308 U.S. 295 (1939). In the particular circumstances, the lenders' inequitable conduct, or other parties' inequitable conduct, arose subsequent to the court's action affording a lien.
13. In addition to equitable subordination, other litigation is possible, if not likely, if the post-petition taxes are not paid. See, *Pacific Insurance Co. v. U.S.*, 270 F.Supp. 165 (N.D. Cal. 1967) (lender who refused to allow its debtor to pay federal taxes and demanded that loan be paid off with any available funds liable for willfully causing non-payment of taxes); NMSA § 7-1-72.1 (any person who causes another taxpayer to willfully evade payment of tax liable for civil penalty equaling 100 percent of the tax, penalty and interest attempted to be evaded).
14. It has been held to be a breach of fiduciary duty when a trustee preferred administrative tax claims to administrative claims of trade creditors, subjecting the Trustee to personal liability. *In re Lambertville Rubber Co.*, 111 F.2d 45 (3d. Cir. 1940) (court ruled that trustee had a fiduciary duty to pay all administrative claims pro-rata if estate was administratively insolvent). There would seem to be no reason

why the same result should not arise if trade creditors and other taxing authorities were preferred over a state tax authority.

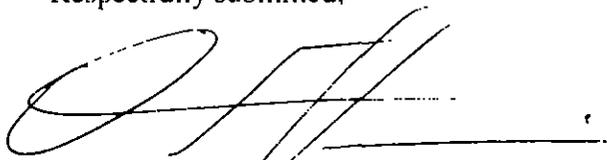
15. "It is well established that a debtor-in-possession is charged with certain duties and obligations upon the commencement of a case under chapter 11 of the Bankruptcy Code. *See*, 11 U.S.C. §§ 1106 and 1107. Primary among these duties is that a debtor-in-possession is a fiduciary to all of its creditors and equity security holders. . . . When a debtor remains in possession, the directors of the debtor corporation bear essentially the same fiduciary responsibilities to creditors and shareholders." *In re Honey Creek Entertainment, Inc.*, 246 B.R. 671, 692 (Bankr. E.D. Okla. 2000).
16. "Indeed, the willingness of courts to leave debtors in possession 'is premised upon an assurance that the officers and managing employees can be depended upon to carry out the fiduciary responsibilities of a trustee.'" *Commodity Futures Trading Commission v. Weintraub*, 471 U.S. 343, 355 (1985) (citation omitted).
17. "It is arguable that the estate trustees may have personal liability for unpaid taxes, at least where available funds were not used for that purpose." *In re Thurman*, 165 B.R. 95, 100 n.6 (Bankr. W.D. Tex. 1994).
18. The Department is entitled to an explanation in this court of equity why the post-petition gross receipts taxes are not being paid. The presumed reason—because the gross receipts taxes are not ordinarily a trust fund liability and that the amount is a lot of money—is not a legal justification. The federal taxes payroll taxes in

the post-petition period for 5000 employees (both trust fund portion and non-trust fund portion) must have been an equally large, if not larger, number.

19. Unlike other creditors, who may have been given assurances by the Debtor and the lenders that the post-petition debts would be paid, the Department had no ability to prevent the Debtor from incurring the liability. Unlike most creditors, the state cannot withhold services unless assurance of tax payment is made.
20. The taxing authority's status as an involuntary creditor is one reason for its preferred treatment in bankruptcy cases.
21. The court should not permit the Debtor, its insiders and the lenders to abuse the involuntary creditor status of the Department and either force the New Mexico taxpayers involuntarily finance Debtors in Possession or allow tax revenues to be transferred (at least in economic terms) to private lenders.

WHEREFORE, no motion seeking to approve any budget should be approved if the budget does not provide for payment of the August gross receipts taxes which are due September 25, 2001.

Respectfully submitted,



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