

UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW MEXICO

FILED
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No. 11-01-10779-SA

In re:

FURR'S SUPERMARKETS, INC.,

Debtor.

**OFFICIAL COMMITTEE OF UNSECURED CREDITORS
OF FURR'S SUPERMARKETS, INC.'S OBJECTION TO FINAL ORDER
(1) AUTHORIZING DEBTOR TO OBTAIN SECURED FINANCING, (2) GRANTING
ADEQUATE PROTECTION AND (3) GRANTING OTHER RELIEF; AND
MOTION TO AVOID LIENS; AND OBJECTION TO CLAIMS OF LENDERS AND
LIQUOR LICENSE SECURED CLAIMANTS**

The Official Committee of Unsecured Creditors of Furr's Supermarkets, Inc. (the "UCC") by and through its local counsel Davis & Pierce, P.C. (William F. Davis, Esq.), for its Objection, hereby STATES:

1. On February 8, 2001 (the "Petition Date"), Debtor (referred to in its prepetition capacity as "Borrower" and in its post-petition capacity as "Debtor") filed a Voluntary Petition for Reorganization under Chapter 11 of the Bankruptcy Code (the "Petition"). Pursuant to §§1107 and 1108 of the Bankruptcy Code, Debtor has retained possession of Debtor's assets and is authorized, as debtor-in-possession, to continue the operation and management of the business previously conducted by the Debtor. The Official Unsecured Creditors Committee of Furr's Supermarkets, Inc., was appointed pursuant to the provisions of §1102 of the Bankruptcy Code (the "UCC").

2. This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157(b)(2) and 1334, and is a core proceeding as defined in 28 U.S.C. §§ 157(b)(2)(A), (B), (K) and (O).

3. On March 14, 2001, the Court entered the "Final Order (1) Authorizing Debtor to Obtain Secured Financing, (2) Granting Adequate Protection and (3) Granting Other Relief" (the "Final Order").

Objection

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4. In the Final Order at Section D, Pages 2-4, the Court made certain findings, inter alia, with regard to the claims of certain secured lenders and creditors of the Debtor (hereinafter, the "Lenders"), as follows:

i. From time to time prior to the Petition Date, Fleet, BofA and Heller (collectively, the "Pre-Petition Senior Lenders") loaned money and issued letters of credit to Borrower pursuant to that certain Loan and Security Agreement dated as of December 21, 2000 (as the same has been amended, the "Existing Loan Agreement") and the other Loan Documents (as defined therein) (the Existing Loan Agreement and the other Loan Documents, collectively, the "Pre-Petition Senior Loan Documents"); as of the Petition Date, the approximate amount owed to Pre-Petition Senior Lenders by Borrower was \$48,107,674.94 (including all Letter of Credit Liability included in the Letter of Credit Reserve, as defined in the Existing Loan Agreement, but exclusive of accrued and unpaid pre-petition interest and costs and fees) (such amount, together with all accrued and unpaid interest, costs and fees, including without limitation, professional fees and expenses and other Obligations under and as defined in the Existing Loan Agreement, collectively, the "Pre-Petition Senior Indebtedness").

ii. Debtor does not contest that pursuant to the Pre-Petition Senior Loan Documents, as of the Petition Date, the Pre-Petition Senior Indebtedness is secured by a continuing first, valid and perfected security interest in substantially all of the existing Collateral (as defined in the Existing Loan Agreement) of Borrower, including, without limitation, all of the Debtor's accounts, inventory, general intangibles, intellectual property, documents, instruments, chattel paper, investment property, stock in subsidiaries, deposit accounts, cash and other property in the possession or under the control of any Pre-Petition Senior Lender, books and records that evidence or contain information relating to such collateral, and all proceeds thereof and continuing valid and perfected security interest in Equipment and all proceeds thereof, second only to the security interest of MetLife described below (collectively, the "Pre-Petition Senior Collateral").

iii. Borrower entered into a Note Purchase Agreement dated as of June 30, 1995 (as the same has been amended and restated, the "1995 NPA"), pursuant to which Borrower issued to MetLife two \$12,500,000 promissory notes; as of the Petition Date, the approximate aggregate amount owed to MetLife by Borrower pursuant to these notes was \$25,000,000, exclusive of accrued and unpaid pre-petition interest and costs and fees (such amount, together with all accrued and unpaid interest costs and fees, including, without limitation, professional fees and expenses, collectively, the "Pre-Petition ML Senior Debt").

iv. Debtor does not contest that pursuant to a Collateral Sharing and Security Agreement dated as of June 30, 1995, as replaced and superseded by a Security Agreement dated as of December 21, 2000, the Pre-Petition ML Senior Debt is secured by a continuing first, valid and perfected security interest in the Equipment of Borrower and all proceeds thereof and a valid and perfected security interest in substantially all of the other Pre-Petition Senior Collateral, second only to the security interest of the Pre-Petition Senior Lenders (collectively, the "Pre-Petition ML

Collateral”).

v. Borrower entered into a Note Purchase Agreement dated as of March 27, 2000 (as the same has been amended and restated, the “March 2000 NPA”) with MetLife and Credit Suisse First Boston Private Equity (“CSFB”) pursuant to which it issued a senior secured note to MetLife in the principal amount of \$8,773,108.90 and to CSFB in the principal amount of \$6,226,891.10; as of the Petition Date, the approximate aggregate amount owed to MetLife and CSFB pursuant to these notes was \$15,000,000, exclusive of accrued and unpaid pre-petition interest and costs and fees (collectively, the “Pre-Petition March 2000 Debt”).

vi. Borrower entered into a Note Purchase Agreement dated as of June 23, 2000 (as amended and restated, the “June 2000 NPA”) with MetLife, CSFB, Windward Capital Associates, L.P. (“Windward”), and management noteholders, pursuant to which the Borrower issued to (a) MetLife a note in the principal amount of \$2,193,277.23; (b) CSFB a note in the principal amount of \$1,556,722.77; (c) Windward a note in the principal amount of \$500,000, (d) Tom Dahlen a note in the principal amount of \$100,000; (e) Steve Mortensen a note in the principal amount of \$50,000; (f) Steven Smart a note in the principal amount of \$50,000; (g) Gene Denison a note in the principal amount of \$20,000; (h) Delwyn James a note in the principal amount of \$30,000; (i) Steve Stork a note in the principal amount of \$50,000; (j) E.G. Gonzalez a note in the principal amount of \$25,000; (k) George Golleher a note in the principal amount of \$100,000; (l) Dick Goodspeed a note in the principal amount of \$200,000; (m) Arthur Typermass a note in the principal amount of \$35,000 and (n) David Morrow a note in the principal amount of \$250,000; as of the Petition Date, the approximate aggregate amount owed pursuant to these notes \$5,160,000, exclusive of accrued and unpaid pre-petition interest and costs and fees (the “Pre-Petition June 2000 Debt”).

vii. Borrower entered into a Subordinated Note Agreement dated as of June 30, 1995 (as amended and restated, the “Subordinated Note Agreement”) with Fleming Companies, Inc., Windward Merchant, L.P., Windward Merban, L.P., Windward/Northwest, L.P. and MetLife pursuant to which the Borrower issued Subordinated Notes (together with the Subordinated Note Agreement, the “Subordinated Debt Documents”) to each of (a) Fleming Companies, Inc. in the principal amount of \$16,142,000.00 (which notes were duly purchased from Fleming Companies, Inc. by the Borrower on June 21, 2000 and canceled); (b) Windward Merchant in the principal amount of \$2,902,114.00; (c) Windward/Merban, L.P. in the principal amount of \$1,934,742.00; (d) Windward/Northwest, L.P. (“Windward/Northwest”) in the principal amount of \$4,836,858.00 (which note was sold by Windward/Northwest, to MetLife prior to the date hereof); and (e) MetLife in the principal amount of \$24,184,286.00; as of the Petition Date, the approximate aggregate amount owed pursuant to these Notes was \$33,858,000, exclusive of accrued and unpaid interest and costs and fees (the “Pre-Petition 1995 Subdebt”).

viii. The Pre-Petition March 2000 Debt, the Pre-Petition June 2000 Debt and Pre-Petition 1995 Subdebt (collectively, the “Pre-Petition Junior Indebtedness”) are subordinated to the Pre-Petition ML Senior Debt and the Pre-Petition Senior Indebtedness pursuant to an Intercreditor Agreement dated December 21, 2000 (the “Intercreditor Agreement”) among MetLife, CSFB,

Windward, the other holders of Pre-Petition Junior Indebtedness party thereto (sic), Borrower and Heller, as agent for Pre-Petition Senior Lenders, and that, in addition, the Intercreditor Agreement sets forth the relative priorities of the liens on the Pre-Petition Senior Collateral and the Pre-Petition ML Collateral and how the Pre-Petition Senior Lenders and MetLife would allocate the proceeds upon sale of such collateral.

All of the definitions contained in the above-quoted paragraphs.(i.) through (viii.) from the Final Order are incorporated by reference herein.

5. The UCC has reviewed the Intercreditor Agreement and objects to the Intercreditor Agreement to the extent it improves the position of Pre-Petition Lenders. The UCC reserves any and all of its claims, rights, causes of action, and allegations with regard to the Intercreditor Agreement until such time as the affect of the Intercreditor Agreement on the distribution of proceeds from collateral can be determined.

6. The UCC has standing and authority to pursue the objections, claims and remedies set forth in this Objection and in the Adversary Complaint filed concurrently herewith pursuant to ¶ 20. of the decretal section of the Final Order at Page 14, in addition to the powers and authorities granted to the UCC in the Bankruptcy Code and Rules, including without limitation 11 U.S.C. §§ 502, 1101 and 1102, and Rule 3007, F.R.Bankr.P. The UCC hereby objects to the Final Order and objects to the claims of the Lenders and the Liquor License Secured Claimants (as defined below), and moves to avoid the claimed liens of the Lenders and the Liquor License Secured Claimants, as follows.

7. All objections raised in the Adversary Complaint filed by the UCC on this date are incorporated as if set out fully herein.

AVOIDANCE OF LIENS OF LENDERS

8. Upon information and belief, and as listed in the Debtor's Schedules filed herein,

the Debtor holds interests in the Leases described in Exhibit 1 hereto. These real property leases and the Debtor's interest in such leases, whether as lessee, sublessee, assignee, or otherwise, are hereinafter collectively referred to as the "Leases." All of the Leases relate to property located in either Texas or New Mexico.

9. MetLife, Fleet, BofA and Heller claim to hold as collateral for secured indebtedness certain liens against the Leases, pursuant to ¶ 6, ¶ 19 and other provisions of the decretal section of the Final Order and the Loan and Security Agreement Dated as of December 21, 2000.

10. Pursuant to Texas and New Mexico law, an interest in a lease is a real property interest, and a security interest in a lease is not perfected until and unless an appropriate financing statement or other appropriate document is filed in the Office of the County Clerk for each county in which real property subject to the lease is located. The Texas version of Article 9 of the Uniform Commercial Code, at V.T.C.A., Bus. & C. § 9.104 1991 (2001 Update), entitled "Transactions Excluded from Chapter," provides in pertinent part:

This chapter does not apply...

(10) except to the extent that provision is made for fixtures in Section 9.313, to the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder;...

See also In re Onley, 48 B.R. 891 (Bankr.N.D.Tex.1985), citing Taylor v. Brennan, 621 S.W.2d 592, 593-4, (Tex.1981). V.T.C.A., Property Code, § 13.002 1991 (2001 Update), entitled "Effect of Recorded Instrument," states:

An instrument that is properly recorded in the proper county is notice to all persons of the existence of the instrument.

11. Section 14-9-1 NMSA 1978, entitled "Instruments affecting real estate; recording," states:

All deeds, mortgages, leases of an initial term plus option terms in excess of five years, or memoranda of the material terms of such leases, assignments or amendments to such leases, leasehold mortgages, United States patents and other writings affecting the title to real estate shall be recorded in the office of the county clerk of the county or counties in which the real estate affected thereby is situated. Leases of any term or memoranda of the material terms thereof, assignments or amendments thereto may be recorded in the manner provided in this section. As used in this section, "memoranda of the material terms of a lease" means a memorandum containing the names and mailing addresses of all lessors, lessees or assignees; if known, a description of the real property subject to the lease; and the terms of the lease, including the initial term and the term or terms of all renewal options, if any.

See also Section 55-9-104(j) NMSA 1978, entitled "Transactions excluded from article," which states: "This article does not apply . . . to the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder;" Cutter Flying Service, Inc. v. Property Tax Dept., 91 N.M. 215, 572 P.2d 943 (Ct.App. 1977) (real property lease is an interest in real property subject to taxation).

12. MetLife, Fleet, BofA and Heller failed to record memoranda of leases, financing statements or any other appropriate documents in the office of the County Clerk for each respective county in which real property subject to the Leases is located.

13. 11 U.S.C. §544, entitled "Trustee as lien creditor and as successor to certain creditors and purchasers," states:

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by--

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial

lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists:

(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

14. 11 U.S.C. § 1107, entitled "Rights, powers, and duties of debtor in possession,"

states:

(a) Subject to any limitations on a trustee serving in a case under this chapter, and to such limitations or conditions as the court prescribes, a debtor in possession shall have all the rights, other than the right to compensation under section 330 of this title, and powers, and shall perform all the functions and duties, except the duties specified in sections 1106(a)(2), (3), and (4) of this title, of a trustee serving in a case under this chapter.

15. Pursuant to 11 U.S.C. §§ 1107 and 544, the Debtor-in-Possession is empowered to avoid any claimed lien on the Leases held by the Lenders. The Lenders are therefore not secured with regard to the Debtor's interest in the Leases, under theories and causes of action including without limitation Lenders' failure to record memoranda of leases, financing statements or any other appropriate documents in the office of the County Clerk for each respective county in which real property subject to the Leases is located, and any purported lien held by the Lenders should be avoided.

16. 11 U.S.C. § 551, entitled "Automatic preservation of avoided transfer," states:

Any transfer avoided under section 522, 544, 545, 547, 548, 549, or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the estate but only with respect to property of the estate.

17. Therefore, as a result of the avoidance of these claimed liens on the Debtor's interest in the Leases, which interest is the property of the Estate pursuant to 11 U.S.C. § 541, the avoidance of the lien or transfer by the Debtor-in-Possession preserves the lien for the benefit of the Estate, and the Debtor holds a perfected first priority lien on the Leases.

MARSHALING

18. As alleged in more detail above, to the extent that the Lenders' claimed liens on the Leases are avoided, and to the extent that the Debtor-in-Possession preserves this position for the Estate and succeeds to the otherwise first priority lien position of the Lenders with regard to the Leases, the Debtor-in-Possession becomes the senior secured creditor with regard to the Leases, and the Lenders remain the senior secured lenders with regard to their remaining collateral. Such remaining collateral personal property and assets of any kind whatsoever, as described in more detail in the Final Order, at ¶ 6 of the decretal section.

19. As a result, the Debtor-in-Possession is the senior secured creditor with regard to the Leases, and is a junior secured creditor, pursuant to the Debtor-in-Possession's strong arm powers, with regard to the remaining collateral. The MetLife, Fleet, BofA and Heller, and their assignees, if any, are senior secured creditors with regard to the collateral other than the Leases, and are junior secured creditors with regard to the Leases.

20. Therefore, based on the facts alleged herein, the equitable remedy of marshaling is appropriate, as follows: (a) two (or more) secured creditors exist, with a common debtor (the pre-petition Debtor, Furr's Supermarkets, Inc.); (b) there are two or more funds belonging to the Debtor, and (c) the Lenders MetLife, Fleet, BofA and Heller, and their assignees, if any, are the senior secured creditors with regard to the remaining collateral other than the Leases, and have

the right to receive payment from more than one fund, while the Debtor-in-Possession, a senior secured creditor with regard to the Leases and junior with regard to the other collateral, can only resort to one fund.

21. Marshaling is not applied if either a senior secured creditor or other parties are prejudiced. No party would be prejudiced, and in fact the unsecured creditors would benefit, if the Lenders MetLife, Fleet, BofA and Heller are required to look to their other sources of funds while the Debtor-in-Possession is allowed to recover on the Leases in order to pay its unsecured creditors.

22. A secured creditor may properly proceed first to collect against "readily available collateral." The senior secured creditor will not be required to proceed first against a fund that requires more rigorous procedures to collect upon if it has a fund more directly available to it that can be easily reduced to money. Therefore, the Lenders MetLife, Fleet, BofA and Heller should be required to look to their more readily available collateral, and the Debtor-in-Possession should be permitted to look to its sole fund for satisfaction of its claim for the benefit of the Estate and the creditors.

AVOIDANCE OF PREFERENTIAL TRANSFERS PURSUANT TO 11 U.S.C. § 547

23. As more fully set out in the Adversary Proceeding filed concurrently herewith, during the ninety (90) days preceding the Petition Date, the Debtor and the Lenders entered into the Pre-Petition Senior Loan Documents with Lenders Fleet, BofA and Heller, referred to herein as the Pre-Petition Senior Lenders, as described in the Final Order at ¶ D.(i), Page 2. This transaction or series of transactions, hereinafter referred to as the Transfer, is or was a preferential transfer pursuant to 11 U.S.C. § 547, and should be avoided as set out in the

Adversary Proceeding.

AVOIDANCE OF LIENS OF LIQUOR LICENSE SECURED CLAIMANTS

24. Upon information and belief, and as listed in the Debtor's Schedules filed herein, the Debtor holds interests in certain Liquor Licenses described in Exhibit 2 hereto. The Debtor's interests in such liquor licenses leases, whether as lessee, sublessee, assignee, or otherwise, are hereinafter collectively referred to as the "Liquor Licenses."

25. Section 60-6B-3 NMSA 1978, entitled "Wholesaler's lien," states:

The transfer, assignment, sale or lease of any license shall not be approved until the director is satisfied that all wholesalers who are creditors of the licensee have been paid or that satisfactory arrangements have been made between the licensee and the wholesaler for the payment of such debts. Such debts shall constitute a lien on the license, and the lien shall be deemed to have arisen on the date when the debt was originally incurred.

26. Certain wholesalers who sold products to the Debtor pre-petition possess a claim of lien on the Liquor Licenses until they are sold. These wholesalers are hereinafter collectively referred to as the "Liquor License Secured Claimants." As provided in Section 60-6B-3 NMSA 1978 *Liquor License Secured Claimants cannot foreclose their interests, compel a sale, or otherwise enforce their claimed liens, until and unless there is a "transfer, assignment, sale or lease" of the Liquor Licenses.*

27. Therefore, pursuant to the Debtor-in-Possession's strong arm powers as set forth above, the Debtor-in-Possession has a superior and senior first position lien on the Liquor Licenses pursuant to 11 U.S.C. § 544, and such lien position is preserved for the estate pursuant to 11 U.S.C. § 551.

28. The UCC requests that the Court enter an Order finding that the Liquor License Secured Claimants are junior secured claimants with regard to the Debtor-in-Possession's

interest in the Liquor Licenses, and that the Debtor holds a perfected first priority lien on the Liquor Licenses, and that such lien is preserved for the benefit of the Estate

WHEREFORE, the UCC, on behalf of the Debtor-in-Possession, respectfully requests that the Court enter an Order:

a. Finding that the Lenders are not secured with regard to the Debtor-in-Possession's interest in the Leases, and that any purported lien held by the Lenders is canceled, released, void, and of no effect, and that the avoidance of the lien or transfer by the Debtor- in-Possession preserves the lien for the benefit of the Estate, and the Debtor holds a perfected first priority lien on the Leases;

b. Awarding the Debtor-in-Possession the equitable remedy of marshaling of assets, and requiring the Lenders to satisfy their claims from collateral other than the Leases;

c. Awarding judgment against Lenders which avoids any transfers described herein pursuant to 11 U.S.C.A. § 547 and avoiding all transfer(s) by Debtor to Lenders in addition to those specifically referred to in this Complaint, if any, which are avoidable under 11 U.S.C.A. § 544, § 545, § 547, § 548, § 549, § 550 or § 553; and for judgment in the amount of any payments deemed to be preferential pursuant to 11 U.S.C. § 547(b)(5), plus interest from the date of the payments, and costs, and judgment disallowing any and all claims by Lenders, or any amounts owed to Lenders according to Debtor's schedules, pursuant to 11 U.S.C.A. § 502(d), unless Lenders have voluntarily released any and all claimed liens on the Leases, and

d. Finding that the Liquor License Secured Claimants are junior secured claimants with regard to the Debtor-in-Possession's interest in the Liquor Licenses, and that the Debtor holds a perfected first priority lien on the Liquor Licenses, and that such lien is preserved for the

benefit of the Estate, and

e. For costs, pre- and post-judgment interest, attorneys fees, and such other and further relief as the Court deems just.

Respectfully submitted,

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The undersigned hereby certifies that a true and accurate copy of the foregoing was mailed this 23rd day of May, 2001.

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