

Ingrid S. Palermo, Esq. (IS-9868)  
HARTER, SECREST & EMERY, LLP  
Local Counsel for City and County of Denver  
1600 Bausch & Lomb Place  
Rochester, New York 14604  
Tel: (585) 232-6500  
Fax: (585) 232-2152

Hearing Date: January 9, 2004 at 10:00 a.m.  
Objections Due: January 8, 2004 at 12:00 p.m.

IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

In re: ) Chapter 11  
)  
ALLEGIANCE TELECOM, INC., )  
et al., ) Case No. 03-13057 (RDD)  
) Jointly Administered  
Debtor. )

---

**LIMITED OBJECTION TO DEBTORS' MOTION FOR ORDERS PURSUANT TO SECTIONS 105(a), 363, 365, AND 1146(c) OF THE BANKRUPTCY CODE (A)(I) FIXING THE TIME DATE AND PLACE FOR THE BIDDING PROCEDURES HEARING AND (II) APPROVING THE NO-SHOP PROVISIONS SET FORTH IN THE ASSET PURCHASE AGREEMENT WITH QWEST COMMUNICATIONS INTERNATIONAL, INC.; (B)(I) ESTABLISHING BIDDING PROCEDURES AND BID PROTECTIONS IN CONNECTION WITH THE SALE OF SUBSTANTIALLY ALL OF THE ASSETS OF THE DEBTORS, (II) APPROVING THE FORM AND MANNER OF NOTICES, (III) APPROVING THE ASSET PURCHASE AGREEMENT SUBJECT TO HIGHER AND BETTER OFFERS AND (IV) SETTING A SALE APPROVAL HEARING DATE; AND (C)(I) APPROVING THE SALE TO QWEST COMMUNICATIONS INTERNATIONAL, INC. FREE AND CLEAR OF ALL LIENS, CLAIMS AND ENCUMBRANCES, (II) AUTHORIZING THE ASSUMPTION AND ASSIGNMENT OF CERTAIN EXECUTORY CONTRACTS AND UNEXPIRED LEASES AND (III) GRANTING RELATED RELIEF**

---

The City and County of Denver ("Denver"), a creditor in the above-captioned bankruptcy case, by and through its local counsel, Harter, Secrest & Emery, LLP, files this Limited Objection to Debtors' Motion For Orders Pursuant To Sections 105(a), 363, 365, And 1146(c)

Of The Bankruptcy Code (A)(I) Fixing The Time Date And Place For The Bidding Procedures Hearing And (II) Approving The No-Shop Provisions Set Forth In The Asset Purchase Agreement With Qwest Communications International, Inc.; (B)(I) Establishing Bidding Procedures And Bid Protections In Connection With The Sale Of Substantially All Of The Assets Of The Debtors, (II) Approving The Form And Manner Of Notices, (III) Approving The Asset Purchase Agreement Subject To Higher And Better Offers And (IV) Setting A Sale Approval Hearing Date; And (C)(I) Approving The Sale To Qwest Communications International, Inc. Free And Clear Of All Liens, Claims And Encumbrances, (II) Authorizing The Assumption And Assignment Of Certain Executory Contracts And Unexpired Leases And (III) Granting Related Relief, (“Motion for Sale”)and in support thereof, states as follows:

1. On or about May 14, 2003 (the “Filing Date”), the debtors (the “Debtors”) filed a petition for relief under Chapter 11 of the Bankruptcy Code.

2. Debtors now propose to sell substantially all of the property of the Debtors as specified in the Motion for Sale, which would alter this bankruptcy from a reorganization to a “liquidating Chapter 11.” To the extent that any of the personal property or cash collateral liened by Denver for taxes is included in the sale, without providing for protection of the proceeds, Denver objects.

3. On or about January 1, 2003 the Debtors had personal property in various Denver locations, which was used in conducting their business and was valued at \$1,434,500.00. This value was the same as assessed in the last property tax statement for the Debtors and attached to Denver’s filed proof of claim dated August 25, 2003 as amended by claim dated December 8, 2003.

4. Personal property taxes for tax year 2003 have been assessed against this personal property in the total amount of \$24,899.68, as evidenced by Denver's amended proof of claim<sup>1</sup>. On January 1, 2004, by operation of law the property was liened by operation of law for the 2004 property taxes. *See*, C.R.S. §§39-1-107, 39-1-105. Colorado law provides a prior and paramount lien against the personal property for this assessment. *See*, C.R.S. §39-1-107. The obligation is enforceable by distraint sale. C.R.S. §39-10-111. The prior and paramount status of personal property tax liens are deemed incorporated into any consensual credit agreements. *See, ITT Diversified v. Couch*, 669 P.2d 1355 (Colo.1983). *See also, Equibank, N.A. v. Wheeling-Pittsburgh Steel Corp.*, 884 F.2d 980 (3<sup>rd</sup> Cir. 1989). Denver is at present fully secured with a priority position over all consensual creditor positions and it would be inequitable to change that status.

5. Denver's Assessor's Office determines the value after January 1, pursuant to C.R.S. §§39-1-104 and 39-1-111. That determination of value for the 2004 tax year is estimated by Denver to be the same as 2003, \$24,899.68, but the actual figure may ultimately be higher or lower than the 2003 value. Denver is only entitled to property taxes based on the actual value for the current year as determined by the Assessor's Office. The fact that the taxes are not currently quantifiable is additional reason to retain Denver's tax lien that is to sell the property subject to the current year taxes, until a final determination of tax is made and paid.

6. The property tax amounts are not specifically addressed in the motion for sale or the sale agreement, although the Debtors appear to indicate an attempt to provide for these taxes

---

<sup>1</sup> The 2002 taxes in the initial proof of claim were paid during the administration of this bankruptcy.

in 4.22 of their agreement. However, Section 4.22 neither specifies the amounts to be set aside nor the taxing authorities to be covered nor does not adequately protect the interests of Denver<sup>2</sup>.

7. Pursuant to Denver Revised Municipal Code (“DRMC”)<sup>3</sup> §§53-25 and 53-38 the sale of Debtors’ personal property located in Denver is subject to Denver sales tax of 3.5%. The sales taxes will be 3.5% of the ultimate sale price garnered by the auction for the personal property of the business. Assuming the value of the Denver Assessor to be correct at \$1,434,500.00, the tax of 3.5% would yield sales tax of \$50,207.50 to be due upon sale.

7. In the instant Motion for Sale, all property is requested to be sold free and clear of all “transfer tax.” There is, as of this Limited Objection, no plan filed. While ultimately a plan may be confirmed and the sale might be under the plan within the meaning of 11 U.S.C. 1146(c), that is not the situation at present. In *Baltimore County Maryland v. Hechinger Liquidation Trust (In re Hechinger)*, 335 F.3d 243, 253-254 (3<sup>rd</sup> Cir. 2003) the Third Circuit held in a well reasoned opinion, that without a confirmed plan in place, sales of a debtor’s assets must be subject to taxation. *Accord, States of Illinois and Washington v. National Steel Corporation*, 2003 U.S. Dist Lexis 15695 (N.D. Ill. 2003). Nonetheless, the Debtors in Paragraphs 46 and 47 of their Motion attempt to invoke the benefit of a confirmed plan when it refers to section 1146(c) of the Bankruptcy Code. There are no securities being sold by Debtor and Denver sales taxes are not similar to a stamp tax. The taxes on the sale of the Debtors’ Denver assets should be paid over to Denver immediately upon sale.

8. Further, Denver’s sales taxes are by law to be paid by the purchaser. It is not in the best interest of the estate or its creditors for the Debtor to make itself liable for a tax for which the purchaser is intended to be liable. *See, Columbine Beverage Co. v. Continental Can*

---

<sup>2</sup> The section references “disclosure schedules” which may or may not clarify the status of taxing authorities and amounts, but Denver was not provided those schedules.

Co., 662 P. 2d 1094 (Colo. App. 1982). Denver remains entitled to 3.5% tax on the sale of assets at the time of closing. The sales taxes are trust fund taxes under DRMC §53-40. As a result of this status, the result is a prior and paramount lien on all property, including the inventory of the taxpayer. *See* DRMC §53-59.

9. Denver's sales tax claims are attached to all property in the Debtor's estate. Denver must be paid from the proceeds of any sale of Debtor's property, including inventory, before any of the proceeds are transferred. The Bankruptcy Code generally expects debtors to comply with local law. The U.S. Supreme Court in *California State Bd. of Equalization v. Sierra Summit*, 490 U. S. 844 (1989) found that the Bankruptcy Code did not intend to disregard local tax law when selling assets of the Debtor. *See also*, 28 U.S.C. §§959 and 960. Thus, if unpaid, the sales tax lien must attach to either the property or the proceeds

10. The proposed Order (I) Approving the Sale Free and Clear of All Liens, Claims and Encumbrances to the Successful Bidder, (II) Authorizing the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases and (III) Granting Related Relief does contain a provision for the priority liens to attach to proceeds of the sale but does not protect the taxing authorities by segregation of those proceeds and by retaining the lien until payment in full is received. Further, the proposed Order does not provide for the payment of sales taxes upon the sale. Denver is entitled to such protections should any of the Denver lien property be subject to the sale.

11. Denver is limiting its objection solely to that property or cash which is subject to Denver tax liens. Denver has no other objection to the Motion.

---

<sup>3</sup> The cited sections of the Denver Code are attached hereto as Exhibit 1 for simplified reference.

12. This limited objection includes citations to the applicable authorities and does not raise any novel issues of law. Accordingly, Denver respectfully requests that the Court waive the requirement in Local Bankruptcy Rule 9013-1(b) for the Southern District of New York that a separate memorandum of law be filed.

WHEREFORE, Denver respectfully requests that this Court deny the Motion to the extent it approves the sale of Debtors' property liened by Denver unless it includes a provision for the payment from the proceeds of the sale or, alternatively, for segregation of proceeds and lien priority of: (a) 2003 taxes of \$24,899.68 and 2004 taxes (currently estimated to be \$24,899.68) for Denver's personal property taxes and maintaining the lien thereon until paid in full; (b) Denver sales tax of 3.5% based on the sale itself; and for such further and equitable relief as to this Court seems just and proper.

Dated: January 5, 2004  
Rochester, New York

HARTER, SECREST & EMERY, LLP  
Local Counsel for City and County of Denver

/s/ Ingrid Schumann Palermo  
INGRID S. PALERMO, ESQ. (IS-9868)  
1600 Bausch & Lomb Place  
Rochester, New York 14604  
Tel: (585) 232-6500  
Fax: (585) 232-2152

