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Judge Mary F. Walrath
Chapter 11
Hearing Date: January 21, 2004
Hearing Time: 9:30 EST
Hearing Location: Wilmington
State's Objection Due: -

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF DELAWARE AT WILMINGTON

In re

FLEMING COMPANIES, INC.,

Debtor.

NO. 03-10945
STATE OF WASHINGTON OBJECTION TO DEBTOR'S DISCLOSURE STATEMENT AND PLAN OF REORGANIZATION

COMES NOW the State of Washington, Departments of Revenue, Labor & Industries and Employment Security, and object to the proposed Disclosure Statement and Plan for the following reasons:

1. Date Certain And Effective Date. The State seeks designation of a date certain as the effective date of the plan, so that no attempt can be made to unduly prolong implementation of payments and so that creditors can ascertain whether the terms of the plan are being complied with. As of now the effective date is subject to conditions subsequent at Article XI which directly implicates feasibility. Even if distributions need to be delayed, interest should run from the eleventh day after confirmation should the plan confirmation not be appealed and stayed pending appeal.

2. No Default Provisions. The plan fails to include appropriate provisions governing default by the debtor under the plan. The State submits that the debtor's plan should contain the following default provision if ultimately any tax payments are to be paid in installments:

> In the event of default by the debtor of any of the provisions of the plan concerning an amount owed to a state tax agency, after 30 days written notice of the

> default and failure of the debtor to cure, the entire amount owed to the tax agency shall be immediately due and owing, and the tax agency may proceed with any remedies otherwise available to it under state law, including but not limited to usual state tax collection procedures, or under federal law, including but not limited to conversion or dismissal under 11 U.S.C. §1112(b).

3. Taxes Not Discharged Until Paid In Full. The Plan fails to provide that tax debts are not discharged until paid in full and that the State's liens remain in effect until the underlying tax claims are paid in full.

4. Debtor Cannot Discriminate Within Tax Class and Pay Cash To Some. The plan discriminates against members of the same class but cavalierly declaring that at "its sole option" some tax creditors might get cashed out on the effective date and some termed out. There is no due process in terms of opportunity for notice and a hearing and contesting such treatment; there are no established criteria for making such a determination and no law supports such action. In order to "cram down" the unclassified creditor group, there must be strict compliance with §1129(a)(9)(C).

5. No "Present Value" Offer Of Payment. The debtor fails to offer established periodic payments and doesn't offer an interest rate. This is a clear failure to adhere to §1129(a)(9)(C).

STATEMENT OF THE LAW

1. ***As Defined in the Plan, "Effective Date" Is Inconsistent with Case Authority and with the Understanding of the Term That Is Integral to the Bankruptcy Code and Rules***

Tax claims that are entitled to priority under 11 U.S.C. § 507(a)(8), like the State's claims here, are deemed "non-classified" and are generally accepted to be non-balloting claims under 11 U.S.C. § 1129(a)(9)(C). The *quid pro quo* for taking away rights that otherwise belong to creditors is that, for a Chapter 11 plan to be confirmed, tax agencies must be paid principal and interest having a present value on the effective date equal to the amount of their claims:

> [T]he holder of such claim [must] receive on account of such claim deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a value, as of the effective date of the plan, equal to the allowed amount of such claim (emphasis added).11 U.S.C. § 1129(a)(9)(C).

Thus the effective date of a plan is a critical element in the valuation and payment of priority tax claims

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"Effective date" is not defined in the Bankruptcy Code or Rules, but it has a well-understood meaning among the bankruptcy bench and bar. Most courts hold the effective date of a plan to be the date when the confirmation order is entered. Tri-Growth Centre City Ltd., 136 B.R. 848, 852 (Bankr. S.D. Cal. 1992).

> [T]his court concurs with the holding in *In re Jones*, 32 B.R. 951 (Bankr. D.Utah 1983), which held that § 1124(a) requires completion of a cure by the effective date of the plan. Although the phrase "effective date of the plan" is not defined by the Code, most courts hold that it is the date of entry of the order of confirmation.

Like the lender in Tri-Growth Centre City, the State in the instant case should not be deprived of its rights under the Code during a long period after confirmation. In In re Wonder Corporation of America, 70 B.R. 1018, 1020, 1021 (Bankr. D.Conn. 1987), the court emphasized that the lack of a definition of "effective date" in the Code was not intended to sanction long intervals between confirmation and effective date:

> Although §1124(3) is silent as to the timing of the effective date, Congress could not have intended to eliminate a creditor's negative vote unless §1124(3) were meant to be read as requiring some reasonable interval between the confirmation order and the effective date of the plan … . Indeed, it is not uncommon for a plan to fix the effective date to a time after the confirmation order is final in recognition of a prospective lender's reluctance to advance funds until the appeal period has passed (emphasis added).

See also, In re Continental Sec. Corp., 188 B.R. 205, 217 (Bankr. W.D.Va. 1995), aff'd, 193 B.R. 769 (W.D. Va. 1996), aff'd, 104 F.3d 359 (4th Cir. 1996).

An effort to delay an effective date to accumulate royalty payments sufficient to pay administrative claims is "highly questionable". In re Applied Safety, Inc., 200 B.R. 576, 581 n.1 (Bankr. E.D.Pa. 1996). The Allied Safety court concurs with the Wonder Corporation court that the "effective date should be the date of confirmation or a date close thereto," and cites 5 Collier on

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Bankruptcy ¶1124.03[7] as support.[1] Similarly, a one year delay between confirmation and effective date in order to buy extra time to collect accounts receivable has been deemed unreasonable, rendering a plan unconfirmable. In re Potomac Iron Works, Inc., 217 B.R. 170, 171 (Bankr. D.Md. 1997). The proposed delay built into the plan has a direct impact on establishing present value for tax claims, as noted in Potomac Iron Works, supra, at 173, citing In re Krueger, 66 B.R. 463, 465 (Bankr. S.D.Fla. 1986).

In In re Krueger, Judge Britton discussed the effect of a smaller gap between confirmation and effective date than the gap in the instant case:

> [T]he date [he] specified is four months in the future. This defeats the purpose of the statutory requirement that the taxing authority receive the equivalent of immediate full payment in cash. The debtor's proposal requires the taxing authorities to partially subsidize the debtor's plan. 66 B.R. at 465.

It is impossible to fairly and accurately value a number of differently classified claims unless the effective date is reasonably close to the confirmation date. See In re Jones, 32 B.R. 951, 958 n.13 (Bankr. D.Utah 1983). In Potomac Iron Works, the court noted the extensive authority for requiring that the effective date of a plan be on or shortly after confirmation:

> Many cases have departed from the "reasonableness" standard for setting the effective date by holding that the effective date should be on or shortly after the date the final order is entered. In support of this proposition is an often cited quotation from an article by Kenneth N. Klee, in an article published shortly after the enactment of the Bankruptcy Reform Act of 1978, entitled, All You Ever Wanted to Know About Cram Down Under the New Bankruptcy Code, 53 Am. Bankr.L.J. 133 (1979): "The 'effective date' of the plan is not a defined term but usually would be the first day after which the order of confirmation becomes final." Id. at 137; see also, 4 Norton Bankr.L. & Prac.2d § 92:17 ("Absent any conditions to the plan, the effective date will often be when the order of confirmation is final").
>
> Recently, Professor Klee urged the proposition that the effective date be set reasonably close to the confirmation date. In an article addressed to the work of the National Bankruptcy Review Commission published in the American Bankruptcy Law Journal in Fall, 1995, Professor Klee recommended:

[1] One court has called it "unusual" for five months to separate the plan confirmation date from its effective date. In re Wills, 226 B.R. 369, 375 n.6 (Bankr. E.D.Va. 1998).

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> A few key provisions of § 1129 of the Code use the term "effective date" of a plan of reorganization without defining it. It is clear to most practitioners and others in the bankruptcy arena that the "effective date" may be a different date than the date of confirmation of the plan, and often plans define the effective date. Nevertheless, it would be useful for the Commission to recommend that Congress enact a provision defining the term "effective date" to be the date on which the provisions of a plan of reorganization become effective and binding on the parties. The statute might also specify that the effective date bear some reasonable relationship to the confirmation hearing date. At the very least, § 1123(a) should be amended to require a plan to define its effective date. This all-important date should not be left to conjecture or undue manipulation. Klee, Adjusting Chapter 11: Fine Tuning The Plan Process, 69 Am. Bankr.L.J. 551, 560-61 (1995). [footnotes omitted] 217 B.R. at 173-74.

Plans that manipulate the effective date premised upon events of asset liquidation months or years in the future directly raise the specter of nonfeasibility and cause many courts to simply deny confirmation. See In re Calvanese, 169 B.R. 104, 107 (Bankr. E.D. Pa. 1994). In addition to the foregoing case authorities, numerous provisions of the Bankruptcy Code and Rules are based upon an understanding that the effective date must be on or shortly after the confirmation date in order to provide meaning to §1129(a)(9)(C). Bankruptcy Rule 3020(e) provides that:

> An order confirming a plan is stayed until the expiration of 10 days after the entry of the order, unless the court orders otherwise.

Why was an order of confirmation made generally subject to an automatic 10-day stay? The committee note explains:

> *Subdivision (e)* is added to provide sufficient time for a party to request a stay pending appeal…..before the plan is implemented and an appeal is rendered moot. Unless the court orders otherwise, any transfer of assets, issuance of securities, and cash distributions provided for in the plan may not be made before the expiration of the 10-day period.Bankruptcy Rule 3020(e)

These comments reflect the common understanding in the bankruptcy community that the effective date should come as soon as the confirmation order is no longer subject to appeal. And, as debtor intends to perform many duties of a reorganized debtor as of the date of confirmation, they have artificially imposed an effective date in a manner that is not legally supportable.

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Bankruptcy Rule 3021 also reflects the general understanding that a plan should become effective as soon as confirmation is final. This rule provides that "after a plan is confirmed, distribution shall be made to creditors whose claims have been allowed … ." Had the Supreme Court, as promulgator of the Rules, believed that the effective date might be a date substantially later than the date of confirmation, it would have referred to the effective date in Rule 3021, and not to confirmation. Finally, the detailed elaboration of the effects of confirmation in 11 U.S.C. § 1141 makes it clear that the order of confirmation is intended to be the effective date. For example, after the confirmation of a plan, the property dealt with by the plan is free and clear of all claims of creditors. 11 U.S.C. § 1141(c). Had Congress expected that there would be protracted delays between confirmation and the effective date, such provisions would logically have been tied to the effective date, not to confirmation.

When interpreting a statute, the court's objective is to ascertain the intent of Congress and give effect to that intent. Moorehead v. United States, 774 F.2d 936, 940 (9th Cir. 1985). It is assumed that the legislative purpose is expressed by the ordinary meaning of the words used. Id.; In re Stainton, 139 B.R. 232, 234-35 (Bankr. 9th Cir. 1992). It is also axiomatic that courts should harmonize statutes and rules when possible so as to not render them meaningless:

> Statutes should generally not be construed to render any provision surplusage. [Citation omitted.] We are required, if possible, to give effect to every word Congress used.

In re Co Petro Marketing Group, Inc., 680 F.2d 566, 569 (9th Cir 1982).

A construction of "effective date" that permits delay eviscerates the provisions of §1129(a)(9)(C) governing treatment of tax claims, and is inconsistent with Congress' intent that the effective date be on or shortly after the date of confirmation. Under the code interest should accrue from the date of confirmation.

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2. ***Discrimination Within The Tax Creditor Class Is Not Permissible Under §1129(b)(1)***

The proposed plan unfairly discriminates within the tax creditor class, arbitrarily stating that some lucky tax creditors get "cashed out" on confirmation while others, under some unstated standard not subject to court scrutiny, will be termed out under §1129(a)(9)(C). And, others are governed by a standard loosely defined as "unless otherwise agreed by the parties". The ambiguity and potential for abuse is palpable. Given the track record of many confirmed Chapter 11 plans it is fair to say tax creditors would see no rational reason to accept "term" payments timed to coincide with distributions to general unsecured creditors when they could be paid in full on confirmation. Any plan confirmation must meet the evidentiary standard imposed by §1129(b)(1). Plan proponent herein has created a single tax creditor classification as **required** by §1129(a)(9)(C) but then proposed disparate treatment within the class with: (1) no evidence of business judgment/factual support; (2) no due process protection on notice and timing of proposed treatment; (3) no due process protection for objecting to proposed treatment; (4) no legal support for the proposition; and, (5) no evidence that the cash payment on confirmation offers the same protection as "term out".

> The classification of claims and interests, as distinguished from the designation of classes, is covered by 11 U.S.C.§1122(a) which permits the placing of claims or interests in a particular class only if such claim or interest "is substantially similar to the other claims or interests of such class". Consistent with this treatment of claims in a particular class is the provision under 11 U.S.C.§1123(a)(4) that the plan must provide the same treatment for each claim or interest in a particular class. [emphasis added] In re Pine Lake Village Apt.Co., 19 B.R. 819, 830 (Bankr. S.D.N.Y. 1982).

If the taxing agency that raises concerns such as those voiced by the State of Washington herein suddenly gets offered "all cash" on confirmation while the laggards stand to get "termed out" how does that equate with "fair and equitable" or non-discriminatory treatment of creditors within the same class? The implication would be that although entitled to be treated equally, the statutory non-balloting class can be compelled to accept disparate treatment by "not speaking up". In analogous circumstances this theory has been rejected and soundly criticized:

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> [3] The Plan in this case fails to comply with Section 1129(a)(9) on its face. The Plan proposes the payment of only 50% of administrative expenses (except for those which have been separately classified, such as professional fees, Dickerson's administrative claim, and the Shorts' administrative claim).
>
> [4] Section 1129(a)(9) provides one loophole to the strict mandate for full payment: the "holder of a particular claim" may agree to a different treatment of its claim. In this ***7** vein, Dickerson argues, citing In re Ruti-Sweetwater, Inc., 836 F.2d 1263 (10th Cir.1988), that if a majority of those claimants in a class who submitted ballots elect to accept a plan, then *all* members of a class are deemed to have accepted the plan under Section 1126(c), and therefore each member is deemed to have *agreed* to waive the right to full payment. Hence, Dickerson argues that because six Class 2 claimants and five Class 3 claimants voted to accept the Plan and no claimants in either class voted to reject the Plan, all members of Class 2 and Class 3 have agreed to accept payment of only 50% of their claims. This Court does not agree. [FN1] In re Digital Impact, Inc., 223 B.R. 1, 6-7 (Bankr. N.D. Okla. 1998).

The court goes on to say:

> This Court concludes that in order to waive the protection of Section 1129(a)(9)(A), a claimant must individually and affirmatively agree to such treatment. *See also* In re Jankins, 184 B.R. 488, 492 n. 8 (Bankr.E.D.Va.1995) (failure of priority claimant to object to treatment less favorable than that required by Section 1129(a)(9) is not consent to such treatment; an affirmative concurrence by the creditor is required); In re St. Louis Freight Lines, Inc., 45 B.R. 546, 552 n. 9 (Bankr.E.D.Mich.1984) (IRS was bound by the plan's treatment, even though less favorable than it was entitled to as a priority administrative tax claimant, because it had "expressly 'approved' the order confirming the plan.").
>
> [5] This reasoning is supported by Section 1123(a)(1) which provides for classification of claims, but specifically excepts from classification claims under Section 507(a)(1)--priority administrative claims. Because these post-petition creditors are entitled to be paid in full, "there is no reason to create a class or classes for such claims in light of the fact that a majority of such classes cannot bind a minority to less favorable payment terms than those provided under section 1129(a)(9)." 7 COLLIER ON BANKRUPTCY ¶ 1129.03 [9][a]. [FN2] Supra, p.7.

The logic and statutory citation is unassailable. Tax creditors entitled to priority for unpaid post-filing taxes under §507(a)(1) and pre-filing tax creditor entitled to priority under §507(a)(8) cannot be "sub-classified" within the single-set class. Any effort to force a waiver of these rights must be through direct, knowing and intentional waiver—not ambush.

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> The Court has a duty to insure an equitable distribution among like claims and sees no legitimate legal or business reason for classifying administrative claims at all, much less in a manner that sets two standards for payment--100% to the plan proponent and professionals who rendered services to the estate, expecting to be paid in full (and 100% to Council Oak in consideration for its withdrawal of its objection to Plan), and 50% to trade creditors and post-petition lenders, who also rendered valuable goods or services to the estate expecting to be paid in full. *See, e.g.,* Boston Post Road Ltd. Partnership v. FDIC (In re Boston Post Road Ltd. Partnership), 21 F.3d 477, (2nd Cir.1994), *cert. denied,* 513 U.S. 1109, 115 S.Ct. 897, 130 L.Ed.2d 782 (1995) (confirmation denied because there was no legitimate reason for separate classification of similar claims); Windsor on the River Assoc. v. Balcor Real Estate Finance, Inc. (In re Windsor on the River Assoc.), 7 F.3d 127, 132 (8th Cir.1993) (one of the primary functions of bankruptcy law is to discourage "side dealing" between debtor and some creditors to the detriment of other creditors); Olympia & York Fla. Equity Corp. v. Bank of New York (In re Holywell Corp.), 913 F.2d 873, 880 (11th Cir.1990) (discretion of plan proponent to classify claims is limited by basic priority rights and cannot be used to manipulate class voting); *see also* 11 U.S.C. § 1122. Supra, p.7 fn.2.

As the court duly notes there is no legitimate legal nor business reason for adding sub-classifications for claims within a single, statutorily authorized class. Clearly, such gamesmanship opens up the opportunity for "side-dealing" that is either intended to be punitive or becomes so, in its detrimental treatment of "other creditors". Manipulation of the Code is neither fair nor equitable—it is discriminatory and insupportable. See also: In re Barney and Carey Co., 170 B.R. 17, 24 (Bankr. D.Mass. 1994).

The promulgators of the Code always envisioned court intervention as to claims classification issues when responding to factual scenarios which were "offensive or abusive". In re Greystone III Joint Venture, 102 B.R. 560, 569 (Bankr.W.D. Tex. 1989) [cites omitted]. More often than not the "gerrymandering" of claims classifications is done for creating balloting advantage, and the predominant number of cases rejecting classification "manipulation" deal with this issue. Whatever flexibility there might be in claims classification must not be found arbitrary nor discriminatory. Supra, p.568. Should there be any doubt as to how the *Greystone* court would come out on priority tax debt, it finds no basis for discriminating as to creditors within a given class. Supra, p.571. It is simply not credible to declare that an all cash payment to "favored" tax creditors bears the equal

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"risk" and "present value" to a "termed out" payment under §1129(a)(9)(C).

CONCLUSION

Like the Three Musketeers, it's all for one, and one for all. Under §1129(a)(9)(C) all taxing creditors get treated the same—identically. There is no "menu of options" like those posited in the present plan. The effective day runs from the eleventh day after entry of the order of confirmation.

DATED this 7th day of December, 2003.

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DATED this _____ day of December, 2003.

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