

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF TENNESSEE
WESTERN DIVISION

IN RE:

MIKE ROSE OIL CO., L.P.,

Debtor.

BK #90-23604-WHB
Chapter 11

MEMORANDUM OPINION AND ORDER ON
OBJECTIONS TO CLAIMS OF
TENNESSEE DEPARTMENT OF REVENUE
AND OF TRAVELERS INDEMNITY COMPANY

In this Chapter 11 case, the Court had previously entered a memorandum opinion and order in adversary proceeding number 91-0006, wherein the Court denied Travelers Indemnity Company's ("Travelers") motion for summary judgment and the Court entered a judgment for the Tennessee Department of Revenue ("Department"). The effect of that judgment was to allow the Department to retain the full penal amount of a petroleum tax bond issued by Travelers. Travelers appealed that judgment and the appeal is pending in the District Court for this judicial district.

At issue in the present opinion are the claims filed in this estate by both the Department and by Travelers. Travelers objected to the allowance of the amended claim filed by the Department in the amount of \$18,725.52. The debtor then objected both to the claims filed by the Department and the claims filed by Travelers. In the alternative, the debtor moved to modify its confirmed plan as to the classification of Travelers. Both Travelers and the Department have responded to the objections and memoranda have been submitted. The issues raised in the objections and motion to modify the plan are core. 28 U.S.C. §157(b)(2)(A), (B), (L) and (O). This memorandum opinion contains findings of fact and conclusions of law pursuant to F.R.B.P. 7052.

FINDINGS OF FACT

1. The Court's opinion and order in adversary proceeding number 91-0006 included certain factual findings, which are incorporated herein by reference. Included in those factual findings was the finding that Travelers issued a petroleum tax bond, number 974G1881-119, in favor of the Tennessee Commissioner of Revenue, which bond had a maximum penal sum of \$86,000.00. By riders, the maximum sum was increased to \$214,000.00.

2. The Department originally filed a claim, number 22, in this estate for \$207,112.48. It later filed claim number 27 for \$6,241.57, and then filed claim number 33 for \$175,003.13. This claim number 33 consisted of prepetition taxes of \$170,655.37, prepetition interest of \$135.65 and prepetition penalties of \$4,347.76.

3. Notwithstanding the amended prepetition claim against the debtor, the Department made demand against Travelers for the full penal sum of its bond, \$214,000.00.

4. In adversary proceeding number 91-0006, the Court concluded that Travelers was contractually obligated to the Department up to \$214,000.00, and that amount has been paid by Travelers to the Department. However, as stated in the preface, the Court's judgment is on appeal.

5. The Department asserts that its claim number 22 was superseded by its lower claim number 33, and that its claim number 33 was superseded by its claim number 38. Also, the Department asserts that its claim number 27 has been superseded by its claim number 34.

6. In summary, the Department's claim number 38 represents its remaining claim against the debtor, after application of the \$214,000.00 bond payment made by Travelers. By an affidavit submitted by the Department, the Department states that it calculated penalty and interest on the debtor's petroleum tax obligation pursuant to Tenn. Code Annot. §67-1-801(a) and §67-1-804(a)(1). The Department then allocated the \$214,000.00 bond payment first to penalties and then to interest, beginning with the oldest obligation. The result of the Department's allocation is that the Travelers' bond did pay some post-petition penalties and interest for which the debtor would not be liable under bankruptcy law, but the remaining amount unpaid, \$18,725.52, does represent prepetition petroleum taxes owing for April, 1990. See, Affidavit of Peggy J.

Hunt, with attached allocation. It is the Department's position that it is entitled to collect the full penal bond from the surety, Travelers, and that the Bankruptcy Code does not control how it applies that bond payment. Further, the Department takes the position that its amended claim number 38 represents only taxes owed by the debtor.

7. As to claim number 27, as amended by claim number 34, the Department states, without dispute, that these claims relate not to petroleum taxes but to sales taxes owed by the debtor for March and April, 1990. Travelers has no surety liability for these sales taxes.

8. The Travelers' bond payment was not applied to the debtor's sales tax liability, and the debtor remains liable for the sales tax liability of \$18,402.09 as represented by the Department's claim number 34. Claim number 34 is an amendment to claim number 27.

9. Claim number 27 was filed on October 15, 1990. The bar date for filing claims was August 21, 1990.

CONCLUSIONS

The Court concludes that Travelers continues to confuse the debtor's tax liability with the surety/contractual liability of Travelers. These liabilities are separate and distinct, and the fact that Travelers is contractually obligated to the Department does not ultimately fix a cap on the debtor's tax liability. While it is true that if there were no surety in this case, the Department could have been allowed only a priority tax claim against the debtor for its prepetition liability of \$175,003.13, this fact does not alter the debtor's liability for that amount. Further, the fact that the Department had a contractual right to look to the surety for its bond liability and the fact that the Department, under applicable state law, applied that bond payment first to penalties and interest does not mean that the Department is evading the Bankruptcy Code. The result of the Department's allocation is to capture from the non-debtor surety its contractual liability and the application of a non-bankruptcy party's liability is not controlled by the Bankruptcy Code. The Department is now asserting a remaining prepetition petroleum tax liability of \$18,725.52 against the debtor. The Court does not find the

Department's procedure to be offensive to the Bankruptcy Code. The Department is not collecting more than its allowable claim from the debtor.

Further, the Court has previously concluded in the adversary proceeding that the debtor's bankruptcy defenses to the Department's claim are not available to Travelers, whose liability arose out of its contract or bond with the Department. The Court found in its earlier opinion that the debtor and Travelers were jointly and severally liable for the petroleum taxes. The debtor has clearly benefitted by the surety's payment of tax liabilities. While the Court can understand Travelers' reluctance to pay its full bond liability, the fact remains that Travelers' delay in payment allowed the post-petition penalties and interest to continue to accrue. It would not be equitable for Travelers to benefit by its delay, however well motivated, by now arguing that the Department should be precluded from allocating Travelers' payment first to penalties and interest.

The Department's claim number 38 is an amended claim reflecting the remaining petroleum tax liability of the debtor. Claims which are filed timely may be amended. The Department's amended claim number 38 is not a late claim. This amended claim is not, as Travelers argues, a materially different claim from the Department's original claim. It is simply the corrected amount of tax liability still owing by the debtor.

As to the priority of Travelers' claims, the Court does not need to address the apparent ambiguity found in 11 U.S.C. §507(d) as to whether it applies to §507(a)(7). See, In re Tentex Marine, Inc., 83 B.R. 530 (Bankr. W.D. Tenn. 1988). Rather, the Court in this particular case may decide the priority of Travelers' \$214,000.00 claim based upon the law of this case and upon judicial estoppel concepts. See, e.g., Stearns Coal & Lumber Co. v. Jamestown R. Co., 141 Tenn. 203, 208 S.W. 334 (1919); Southern Coal & Iron Co. v. Schwoon, 145 Tenn. 191, 239 S.W. 398 (1921); Loftis v. Stuyvesant Insurance Co., 54 Tenn. App. 371, 390 S.W. 2d 722 (1964); Gilley v. Jernigan, 597 S.W. 2d 313 (Tenn. Ct. App. 1979). In its earlier summary judgment opinion in adversary proceeding number 91-0006 the Court understood that, notwithstanding §507(d), the debtor and Travelers had agreed that Travelers would be paid \$175,003.13 of its claim as a priority claim. Further, the debtor entered into a postpetition agreement wherein the debtor acknowledged its

liability to the Department for \$175,003.13, the Department's prepetition petroleum tax claim, and the debtor, in that document, agreed for Travelers to pay that amount of the tax claim. See, Exhibit E to Amended Complaint in adversary proceeding number 91-0006. Travelers subsequently filed a priority proof of claim, and Travelers voted its acceptance of the debtor's plan as a priority creditor in Class II. It is true that the debtor did not specifically state in its written agreement or in its plan that Travelers would be treated as a priority creditor, but the order of confirmation dated December 26, 1990, provides that Class II had accepted the plan. Travelers was the only creditor voting in that class. The Court can not ignore now the fact that Travelers accepted based upon its Class II ballot. Obviously, Travelers was of the understanding that it would be so treated. In its Addendum to Disclosure Statement, the debtor stated that it will "dispute any claim of Travelers Indemnify Corporation [sic] as duplicative of the State of Tennessee." Obviously, Travelers has satisfied the largest portion of the state's petroleum tax claim and there is no existing duplication of claims. Finally, the debtor on April 22, 1991, filed its answer and objection to Travelers' motion for default and summary judgment in adversary proceeding number 91-0006, in which pleading the debtor stated that it would agree and stipulate that Travelers was entitled to a prepetition priority claim of \$175,003.13. Contrary to the debtor's position now, that pleading, taken together with all of the other facts, circumstances, and equities of this specific case does judicially estop the debtor from changing its agreement. Such a position change would simply be unfair to Travelers that relied upon the debtor's agreement.

The Court commends the debtor for taking a present position that obviously demonstrates that the debtor is not engaged in a conflict of interest with its principal partner, Michael L. Rose. Mr. Rose is a debtor in a separate Chapter 7 case, number 90-30633-B and in that case Travelers has filed an adversary proceeding, number 91-0441, to determine whether the petroleum tax obligations paid by Travelers are excepted from his discharge under §523(a)(1). A summary judgment motion is pending in that proceeding. Obviously, Mr. Rose has potential individual exposure to Travelers, which potential exposure would be reduced to the extent that Travelers receives priority payment in this partnership case.

The debtor's counsel represented to the Court at oral argument on October 7, 1991, that \$109,000.00 was on hand to pay Class II priority creditors. However, the debtor now asks for permission to modify its plan to reclassify Travelers into Class XII as unsecured. Based upon the Court's conclusion that the debtor is estopped from altering its agreement to treat Travelers as a priority claimant, it would be inconsistent for the Court to grant the debtor's motion to modify the confirmed plan. Furthermore, the Court understands that administrative expenses have been paid subsequent to the confirmation, which payments may constitute substantial consummation of the confirmed plan. See 11 U.S.C. §1127(b). It would be unfair for the debtor to benefit from a December 26, 1990 confirmation order, to pay its counsel, and then to expend further funds in a modification effort and in a new, likely contested, confirmation effort. The result could be that all of the debtor's assets would be spent in professional fees and the priority creditors would receive less, if anything. The debtor's motion to modify its confirmed plan is denied.

AMOUNT OF PRIORITY CLAIMS

The Court concludes that the Department's claim number 38 in the amount of \$18,725.52 is allowed as a priority tax claim against the debtor. As to Travelers' claims for Tennessee petroleum taxes, only \$175,003.13 can be a priority claim since the priority is limited to the amount to which the debtor would be obligated to the state. Further, the facts and circumstances of this case dictate that the Department be paid first its \$18,725.52 so that the debtor's prepetition tax liability is paid in full. After that payment, to the extent money is available, Travelers will be paid a priority payment for the Tennessee petroleum tax up to \$156,277.61. This result would allow a total priority prepetition Tennessee petroleum tax claim of \$175,003.13, which is all that the debtor can owe. The balance of Travelers' Tennessee petroleum tax claim will be allowed as an unsecured claim. This result is consistent with the Court's conclusion that Travelers' obligation on the petroleum tax bond is contractual and is a separate liability from that of the debtor. Travelers has further amended its claim to reflect that it paid \$11,892.75 in prepetition Kentucky petroleum taxes and that claim is allowed as a priority claim to be paid after Tennessee's \$18,725.52 priority claim is paid. Travelers may decide whether it wants this \$11,892.75 paid prior to its \$156,277.61 payment, if

insufficient funds are available for full priority payment. The balance of Travelers' Kentucky petroleum tax payment, \$14,103.67, is allowed as an unsecured claim.

The Court notes that an order approving final fees to the debtor's counsel was entered on August 6, 1991. Under all of the circumstances of this case, no further attorney's fees will be allowed for the debtor unless all priority creditors are paid in full. It is fair and just that the priority creditors be paid promptly and that this liquidating case come to a rapid close. The Court will order, therefore, that within eleven (11) days from the entry of this order the debtor is to make the payments to the priority creditors. Should there be priority creditors in addition to the Department and Travelers and should there be insufficient funds to pay them in full, counsel for the priority creditors shall confer in an effort to reach an agreement on an equitable pro-rata distribution. If such an effort fails, the parties should immediately move the Court to conduct a settlement conference, at which time counsel for all priority creditors must be present.

Based upon the debtor's objection to the Department's sales tax claim number 27, as amended by number 34, as being late, and there being no apparent dispute about that fact, the Department's sales tax claim number 27, as amended by number 34, is allowed as a late claim to be paid after all other allowed priority claims are paid, to the extent funds are available for payment of priority claims.

IT IS SO ORDERED this 24th day of March, 1992.

WILLIAM HOUSTON BROWN
UNITED STATES BANKRUPTCY JUDGE

cc:

Toni Campbell Parker
Apperson, Crump, Duzane & Maxwell
Attorney for the Debtor
2110 One Commerce Square
Memphis, Tennessee 38103

Scott A. Frick
Less & Scroggs
Attorney for Travelers Indemnity Company
80 Monroe Avenue
Suite 900
Memphis, Tennessee 38103

Brendan Bradley
Attorney for Tennessee Department of Revenue
1240 Andrew Jackson Building
500 Deadrick Street
Nashville, Tennessee 37212

Madalyn Scott
Attorney for U.S. Trustee
200 Jefferson Avenue
Suite 400
Memphis, Tennessee 38103

(Published)