

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

IN RE:)
)
CONTINENTAL SALES & ENGINEERING, CORP.) CAUSE NO: 10-02648-JKC-11
)
DEBTOR.)
_____)

**FIRST DAY MOTION REQUESTING
AUTHORITY TO PAY EMPLOYEE
COMPENSATION AND BENEFITS**

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE:

In support of the above entitled motion (the “Motion”), Continental Sales & Engineering, Corp., the debtor and debtor-in-possession (the “Debtor” or “Continental”), by counsel, states:

A. JURISDICTION

1. The Debtor filed its petition for relief under Title 11, Chapter 11 of the United States Code on March 4, 2010 (the “Petition Date”).

2. This Court has jurisdiction over this Motion and this matter pursuant to 28 U.S.C. §157(b). Venue of this case and this Motion in this district is proper pursuant to 28 U.S.C. §§ 1408 and 1409. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2).

3. The statutory predicates for relief are §§103, 105(a), 363(b)(1), 363(c)(1), 507(a)(4), 507(a)(5), 1106, 1107(a), 1108 and 1129(a)(9) of the of the Bankruptcy Code, codified at 11 U.S.C. §101, *et seq.* (the “Code”).

B. BACKGROUND

4. Since the Petition Date, the Debtor has continued in the possession of its property pursuant to 11 U.S.C. §§ 1107 and 1108, and is a debtor-in-possession. No trustee or examiner has been appointed in this case. No committees have been appointed or designated.

5. The Debtor was founded in 1952 by Douglas M. Miles, Sr. The Debtor is in the business of distributing parts to primarily automotive manufacturers and designing and selling integrating service. Parts the Debtor commonly sells includes: masking, safety supplies, abrasives, cutting tools, gear cutting durable items, specialty tooling, coolants, hand tools, OEM Spares and parts or work holdings, vending machines, machinery and MRO supplies for a variety end users. The Debtor also provides the following services: engineering, cost reduction and process improvements, training, education, benchmarking, repair programs, minority programs, crib management, integrated supply and inventory control. The Debtor fills a rare niche in the engineering industry.

6. The Debtor provides for customers elimination of machine down time, increase manufacturing productivity, reduce cost per piece produced where applicable, reduce/eliminate in-plant tooling inventory, reduce obsolete tooling, minimize/eliminate “Emergency/Rush Deliveries”.

7. The Debtor operates from corporate headquarters located at 10201 N. Hague Road, Indianapolis, Indiana, 46256 and at four other locations: Rocky Mountain, North Carolina, Charleston, South Carolina, McDonna, Georgia, and Columbus, Indiana.

8. The Debtor intends to reorganize in this proceeding, and this case was filed as an emergency because it’s banks accounts were garnished by a judgment creditor.

9. The Debtor operates from corporate headquarters located at 10201 N. Hague Road, Indianapolis, Indiana, 46256.

10. The Debtor generated approximately \$7,353,805.00 in gross revenue in 2009 and anticipates it will generate approximately \$6,600,000.00 in gross revenue in 2010.

11. The Debtor intends to reorganize in this proceeding.

12. The Debtor's records show that there are 18 full-time and 6 hourly, non-officer/non-director/non-owner employees of the Debtor (the "Employees"). None of the Employees are "insiders" or "equity security holders" of the Debtor, as those terms are defined in the Code. As of the Petition Date, the Employees were owed by the Debtor, or had accrued in their favor: (i) wages; (ii) salaries; (iii) commissions; (iv) reimbursements for business expenses; (v) vacation pay (the "Compensation"). In addition to the Compensation, the Debtor also provides some or all of its Employees with the following benefits: health insurance (the "Benefits"). As of the Petition date, the Benefits were paid and current through the end of March 2010. Worker's Compensation is paid monthly to Cincinnati Insurance Companies (the "Worker's Comp.")

13. The Employees may receive health insurance as a Benefit of their employment with the Debtor. Six of the Employees are currently provided health insurance. Four of the Employees are provided 100% health insurance coverage. One Employee is provided 72.9% and another is provided 27.6% health insurance coverage. As of the Petition Date, all insurance is paid and current through March 2010.

14. The Debtor pays six (6) of its Employees on an hourly basis, as wages, and eighteen (18) of its Employees on salary. The Debtor pays its hourly Employees and its salaried Employees bi-weekly. All wages and salaries paid to Employees have accrued by the payroll date. As of any payday when the hourly Employees are compensated for their wages, these Employees are paid one

week in arrears. As of any payday when the salaried Employees are compensated, these Employees are paid salary current on said payday. Debtor issues payroll to employees in the form of paper checks. The Employees are paid on Fridays.

15. Employees also receive vacation pay, which accrues as follows on each Employee's hiring date anniversary: (i) After working one year for Debtor – 1 week of vacation; (ii) After working 2 years for Debtor – 2 weeks of vacation; (iii) After working 5 years for Debtor – 3 weeks of vacation; (iv) After working 10 years for Debtor – 4 weeks of vacation.

16. Some of the Employees (i.e. those Employees who are in sales) are paid commissions in addition to their salary. These Employees accrue commissions on a "pay when paid basis." This means that the commissions accrue for the Employees on the day when the customer pays for the rental or purchase of the equipment. The Employees are paid their commissions one month in arrears, and the commissions are paid with the second pay check for the month.

17. Five of the Employees receive a vehicle allowance, in addition to their salary, as a Benefit. The vehicle allowance is a pre-established amount of \$500.00, paid with the first pay check of each month to the Employee. The total amount of the vehicle allowance, which is paid by the Debtor each month as an Employee Benefit, is \$2,500.00. As of the Petition Date, all payments for the vehicle allowance are current and there are no pre-petition payments for the vehicle allowance Benefit due and owing to the Employees.

18. Some of the Compensation due certain one of the Employees is subject to garnishment orders and child support orders, which the Debtor is legally obligated to honor. Child support payments are paid via the Debtor, and a check is mailed on the Friday payday. Garnishments are processed internally and paper checks are issued on Friday payday.

19. In addition to the payroll, the Debtor the following taxes which are also funded on the Friday payday: (i) Federal withholding; (ii) State withholding; (iii) Local withholding; (iv) FICA (social security); (v) SUTA (state unemployment tax); and (vi) FUTA (federal unemployment tax). Debtor then pays the funds to the appropriate taxing authority on the date on which said taxes are due and owing. The taxes will be paid in the Debtor's ordinary course of business.

20. Benefits and Worker's Comp. are processed internally by the Debtor. Health insurance and Worker's Comp. are paid as invoiced. As previously stated, all Benefits and Worker's Comp. are current, and there are no Benefits due and owing to the Employees. Worker's Comp. is paid quarterly and has not been audited for the first quarter of 2010.

C. CURRENT COMPENSATION AND BENEFITS

21. The Debtor's most recent payroll was paid to Employees on Friday, March 5, 2010, for the period February 13, 2010 through February 27, 2010 for the hourly wage Employees, and the period of April 4, 2009 through April 17, 2009 for the salaried Employees (the "February 27 Payroll"). The February 27 Payroll was paid prior to the filing of the petition in this case.

22. As of the Petition Date, pre-petition wages and salaries that were paid to the Employees by personal deposit of the owner, Douglas M. Miles, Sr. (the "Owner"). The approximate \$44,000.00 in gross payroll was paid to Employees on March 5, 2010 for pre-petition Compensation of the February 27 Payroll. The Debtor's next payroll for its Employees is scheduled for Friday, March 19, 2010. On that date Employees will be paid approximately \$44,000.00 for the period of February 28, 2010 through March 13, 2010 (the "March 13 Payroll").

23. The Compensation for the February 27 Payroll was paid post-petition and the March 13 Payroll is due and owing after the Petition Date because the Chapter 11 petition was filed in the middle of the Debtor's regular and customary wage payroll period.

24. The Benefits owed as of the Petition Date are paid at the beginning of each month in advance for that month. Prior to the Petition Date, the Debtor paid the Benefits for the month of March. As of the Petition Date, it can be said there are no pre-petition benefits due and owing to the Employees.

D. INSIDER COMPENSATION AND BENEFITS

25. The insiders (as that term is defined in the Code) of the Debtor as of the Petition Date are Douglas Miles Jr., Ryan Miles, and Brett Miles (collectively, the "Insiders").

26. As of the Petition Date, the Insider was paid Compensation in the form of salary follows: a) Douglas Miles Jr., bi-monthly in the amount of \$10,000.00; b) Ryan Miles, bi-monthly in the amount of \$3846.15; and c) Brett Miles, bi-monthly in the amount of \$2692.30. As of the Petition Date, the Insiders' salaries are current. The Insiders' annual salaries are as follows: 1) Douglas Miles Jr. \$240,000.00 plus commission; 2) Ryan Miles \$100,000.00; and 3) Brett Miles \$70,000.00.

27. As of the Petition Date, there were no Benefits owed the Insiders. The Worker's Comp. and all insurance are current, because insurance requires payment for Benefits on the 1st day of the month and Worker's Comp. has not yet been audited. The insiders are not owed any other Compensation. The Insiders are not owed any salary or commissions.

E. CASH COLLATERAL

30. The money to be used to fund all payments of Compensation and Benefits is the cash collateral of Busey Bank ("Busey").

F. ANALYSIS

31. To the best of Debtor's knowledge, the total Compensation¹ due and owing by the Debtor to all on the Petition Date, does not exceed the sum of \$10,950.00, the limitation mandated by §507(a)(4) of the Code, which grants a priority claim for each individual for wages earned within 180 days before the Petition Date for:

(A) wages, salaries, or commissions, including vacation, severance, and sick leave pay earned by an individual; or

(B) sales commissions earned by an individual . . .
11 U.S.C. §507(a)(4).

The Debtor is not seeking to pay said Employee (including Insiders) more than the statutory limit of \$10,950.00 with this Motion. The Debtor is only seeking authority to pay each Employee and Insider the amount earned on the Petition Date, but not to exceed the statutory limitation of \$10,950.00. Additionally, the Debtor does not intend to pay any Employee or Insider for his or her accrued vacation pay in cash. Instead, the Debtor will allow the Employees to use the vacation pay accrued pre-petition for post petition paid days off from work.

32. To the best of Debtor's knowledge, the total contributions for Benefits due and owing by the Debtor to Employees does not exceed the statutory limitation established by § 507(a)(5) of the Code. Moreover, as of the Petition Date, there are no benefits due and owing to any Employee. Section 507(a)(5) of the Code, grants a priority claim for contributions to an employee benefit plan--

(A) arising from services rendered within 180 days before the date of the filing of the petition or the date of the cessation of the debtor's business, whichever occurs first, but only

(B) for each such plan, to the extent of--

¹ Including any and all accrued wages, salary, commissions, for the February 27 Payroll, March 13 Payroll.

(i) the number of employees covered by each such plan multiplied by \$10,950; less

(ii) the aggregate amount paid to such employees under paragraph (4) of this subsection, plus the aggregate amount paid by the estate on behalf of such employees to any other employee benefit plan. 11 U.S.C. §507(a)(5).

33. The Debtor submits that good cause exists for authorization of the payment of Compensation and Benefits as described herein to all of its Employees and Insiders in the normal course of the Debtor's business, in that the Employees and Insiders are essential and vital to the Debtor's continuing operations, and one missed payroll will likely result in many Employees leaving the employment of Debtor. Any delay in paying the Compensation and Benefits will severely disrupt the Debtor's relationship with its Employees and irreparably impair their morale at the very time when their dedication, confidence and cooperation are most critical. There is no justifiable reason Insiders should not be paid as well because they work along with Employees.

34. The Debtor must continue its corporate policy of permitting certain of its Employees to incur business related expenses and thereupon seek reimbursement thereof by submitting an expense report containing the appropriate invoices or vouchers evidencing said out-of-pocket disbursements. Finally, were the relief requested herein not to be granted, the Employees would suffer great hardship and, in many instances, financial difficulties, since the monies are needed to enable them to meet their own personal obligations.

35. The Debtor seeks authorization to pay the Compensation and Benefits that accrued in the normal course of the Debtor's business prior to the Petition Date, but are due in the normal course of the Debtor's business only after the Petition Date. This includes continuing to honor all garnishments and child support orders. It also includes continuing to honor accrued vacation pay up to the maximum amount allowed by §507(a)(4) of the Code. Further, this includes seeking an

order clarifying that any payment of Compensation or Benefits, so long as it is detailed herein and the Debtor is authorized to pay it, that accrued prior to the Petition Date and was paid prior to the Petition Date, but only processed after the Petition Date or was paid and processed after the Petition Date is not a preference under §547, a transfer under §548 or a post petition payment under §549; otherwise, Employees must worry about paying back their Compensation or Benefits.

36. In order to maintain the continuity of the Debtor's business, and to preserve the morale of the continuing labor force, it is essential that the Debtor be permitted to pay to the Employees the Compensation and Benefits which have accrued but which remain unpaid as set forth herein. It cannot be over-emphasized that the Employees are being asked to apply their time and energies to the efforts to continue operation of the business with renewed and even greater vigor. It is clearly in the best interests of the Debtor and its creditors that approval of the payments sought herein for Compensation and Benefits be made so as to avoid hardship to the Employees and also to maintain and preserve the viability of the Debtor's ongoing business.

37. Courts have recently granted similar relief to the relief requested in this Motion in other cases in the Seventh Circuit². The Seventh Circuit's decision In re Kmart Corporation, 359 Fed. 3d 866 (7th Cir. 2004), is distinguishable, and does not prohibit the Debtor from being permitted to pay payroll as requested herein. In Kmart, the Seventh Circuit upheld a district court ruling denying the Debtor permission to make critical vendor payments. The Court found that §105(a) of the Code, by itself, does not provide authority to make critical vendor payments, as

² See, for example, In re Buehler Foods, Inc., Cause No. 05-70961-BHL-11 (Bankr. S.D. Ind. 2005); In re ATA Holdings Corp. et al., Cause No. 04-19866-BHL-11 (Bankr. S.D. Ind. 2004); In re Paul Harris Stores, Inc., Cause No. 00-12467-BHL-11 (Bankr. S.D. Ind. 2000); In re Jays Foods, L.L.C., Case No. 04-08681 (Bankr. N.D. Ill., 2004); In re FV Steel and Wire Company, et al., Case No. 04-22421 (SVK) (Bankr. E.D. Wis., 2004); In re National Equipment Services, Inc., Case No. 03-27626 (PSH) (Bankr. N.D. Ill. 2003); In re Eagle Food Centers, Inc., Case No. 03-15299 (PSH) (Bankr. N.D. Ill. 2003); In re UAL Corp., Case No. 02-48191 (ERW) (Bankr. N.D. Ill. 2002); In re Kmart Corp., Case No. 02-02474 (SPS) (Bankr. N.D. Ill. 2002).

the bankruptcy Court had solely relied on. The Court left open the issue of whether §363(b)(1), in conjunction with §105(a) of the Code could provide support for paying critical vendors.

38. The holding of the Kmart decision is not binding on the particular relief being sought in this Motion and moreover is easily distinguishable from this case, both on its facts and on the law. It is not binding because the Debtor in Kmart relied solely upon §105(a) as the statutory basis for relief whereas here the Debtor relies upon §105(a) in conjunction with other Code sections, including §§103, 363(b)(1), 363(c)(1), 507(a)(4), 507(a)(5), 1106, 1107(a), 1108 and 1129(a)(9).

39. Section 105(a) of the Code provides that “[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title.” § 105(a). The purpose of §105(a) is “to assure the Bankruptcy Court’s power to take whatever action is appropriate or necessary in aid of the exercise of its jurisdiction.” 2 Collier, Bankruptcy ¶ 105.02, at 105-4 (15th rev. ed. 1988). Thus, §105(a) of the Code essentially codifies the Bankruptcy Court’s inherent equitable powers.

40. Section 363(b)(1) of the Code provides a mechanism for the debtor to use property of the estate out of the ordinary course (of distribution under the Code). Section 363(c)(1) of the Code provides a mechanism for the debtor to use property of the estate in the ordinary course (of distribution under the Code). Debtor submits the relief requested herein is within the ordinary course. Sections 507(a)(4) and 507(a)(5) of the Code provide for payment of employee wages and benefits on a priority basis. Sections 1106, 1107 and 1108 of the Code provide that a debtor in possession has the powers of a trustee to operate on ongoing business, including “an implied duty of the debtor-in-possession to ‘protect and preserve the estate, including an operating business’ going-concern value” In re: CEI Roofing, Inc., 315 B.R. 50, 59 (Bankr.N.D. Tex 2004) (*citing In re*

Coserv, L.L.C., 273 B.R. 487, 497 (Bankr.N.D.Tex.2002)). Section 1129(a)(9) reinforces the priority scheme of §507 that provides a priority under the Code for the payment of Compensation and Benefits.

41. Kmart is further distinguishable in that this Motion seeks Court authority to pay employee payroll and benefits (which are accorded priority status under the Code), not “critical vendors” (which are not accorded priority status under the Code). Succinctly stated by a recent bankruptcy Court, which analyzed the Kmart decision, and nonetheless granted a first day motion to pay employee payroll in a chapter 11 case:

[t]hus, there has evolved a rule for the payment of prepetition wages and benefits which is based on both common sense and the express provisions of the Bankruptcy Code. If employees are not paid, they will leave. If they leave the Debtor’s business, the bankruptcy case fails shortly after the filing. No one will benefit from the process. The Code gives employees a statutory priority that elevates the claims above the general unsecured claims, and, in fact, most claims in the bankruptcy case. To the extent that the existing holders of claims of higher priority than the wage claims consent or do not timely object, such priority claims may be made during the pendency of the bankruptcy case. The treatment and payment of such claims before confirmation does no violence to the Code or existing case law in this Circuit. In fact, such orders are usually “necessary” and “appropriate” to implement a debtor’s reorganization under Chapter 11. CEI Roofing, Inc., 315 B.R. at 61.

42. **Statement pursuant to L.R. B-9013-3(b).** On March 8, and prior to filing this Motion, below signed counsel discussed its general contents with counsel for the United States Trustee, Laura DuVall, in the form of voicemail left for counsel, who was out of the office that day. Although below signed counsel was unable at that time to provide detailed specifics regarding the Motion, an offer was made to confer prior to a hearing regarding any questions counsel for the U.S. Trustee may have regarding the Motion.

Request for Relief

The Debtor respectfully requests the Court grant this Motion and for all just and proper relief in the premises.

Respectfully submitted,

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/s/ Jeffrey M. Hester

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