

Bankruptcy Law

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By Alex Wolf

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1. Bankruptcy court sustains bulk of suit to claw back dividends
2. Investors loaded company with debt in years before bankruptcy

A Morgan Stanley unit and other previous owners of Tops Friendly Markets must face the bulk of a lawsuit accusing the investors of rendering the grocery chain insolvent while paying themselves \$375 million in dividends.

A trust formed out of the 2018 bankruptcy plan for Tops Holding II Corp. can continue pressing claims against Morgan Stanley and other private equity investors to recoup funds for Tops' unsecured creditors, Judge Robert Drain of the US Bankruptcy Court for the Southern District of New York ruled in a 109-page opinion Wednesday.

Morgan Stanley Investment Management Inc., HSBC Private Equity Partners USA and other defendants argued that the claims were flawed in a number of ways, and were otherwise implausible or time-barred.

But Drain said that the fraudulent transfer claims were sufficiently pleaded and can move forward to be decided on the merits.

The judge, however, dismissed two claims asserting breach of fiduciary duty against two Morgan Stanley directors who served on the board for Tops and dismissed a claim against Morgan Stanley "for aiding and abetting breach of fiduciary duty."

"We are happy with the decision and look forward to prosecuting the case for the benefit of the creditors of Tops," Kyle Lonergan of McKool Smith, an attorney for trustee Alan Halperin, said in a statement.

Morgan Stanley declined to comment.

Morgan Stanley's private equity unit led a group to acquire the New York-based grocery chain in 2007 for \$300 million. Over the course of six years before selling the company, the private equity investors allegedly loaded the company up with debt while ignoring employee pension plan liabilities that grew from \$85 million upon the acquisition to over \$515 million.

Halperin alleged in a 2020 complaint that the investors over-leveraged the company and took "massive, illegal dividends" worth \$375 million, contributing to the chain's insolvency.

Tops won approval to reorganize in bankruptcy in late 2018, giving equity and new secured loans to its lenders.

The case is Halperin et al. v. Morgan Stanley Investment Management Inc. et al. , Bankr. S.D.N.Y., No. 20-08950, opinion 10/12/22 .

To contact the reporter on this story: Alex Wolf in New York at awolf@bloomberglaw.com

To contact the editor responsible for this story: Maria Chutchian at mchutchian@bloombergindustry.com

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