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Morgan Stanley Tells Court It Sold A Solvent Tops Markets

By **Rick Archer**

Law360 (September 10, 2020, 10:25 PM EDT) -- Morgan Stanley on Thursday asked a New York bankruptcy judge to dismiss claims by the litigation trustee for Tops Markets LLC that the firm drove the supermarket chain into Chapter 11, arguing the company was solvent when the firm sold it.

Morgan Stanley offered U.S. Bankruptcy Judge Robert Drain multiple reasons for dismissing the fraudulent transfer and breach of fiduciary duty claims, spending much of the nearly five-hour remote hearing denying claims Tops was insolvent when it paid out \$375 million in dividends under Morgan Stanley-led ownership.

A Morgan Stanley-led group of private equity investors bought Tops in 2007 for \$300 million, \$227 million of that funded by debt issued by Tops, and sold it in 2013 to a group of Tops executives for \$21 million. The company filed for Chapter 11 in February 2018, and Judge Drain approved a \$455 million reorganization plan that November.

A litigation trust was established, and in February trustee Alan Halperin filed suit alleging Morgan Stanley drove Tops into bankruptcy by causing it to pay out more than \$375 million in "lavish and illegal dividends" while running up \$426 million in debt and leaving the company with \$515 million in liabilities from underfunded pension plans.

Morgan Stanley, along with other investors and individual directors named in the suit, had moved for dismissal on grounds including arguments that, contrary to Halperin's claims, the company was solvent when the dividends were paid.

Morgan Stanley counsel Pamela Miller argued Tops had the "indicia of solvency" through 2013 and beyond, saying it continued to operate for nine years after the first dividend payment and was able to take out loans at "decreasing interest rates."

She also argued it was "simply implausible" that the management team would put \$4.6 million of their own money into buying an insolvent company.

"They had full knowledge, better than anybody, of Tops' operations and financial status," she said.

Judge Drain, however, said there were potentially "a lot of reasons" to invest in a company that don't involve belief in its solvency.

"People put money into insolvent companies because they think they can turn them around. It happens all the time," he said.

Miller also argued that Halperin had improperly used the full amount of withdrawal liability for a multicompany Teamsters pension fund as part of its solvency calculations. She claimed Tops would only had to have paid the full amount if the fund collapsed and that therefore a discount should be applied to the liability.

"Tops had adequate capital when it was contributing and would have had the capital to make those contributions if it had to withdraw," she said

Kyle Lonergan, one of the counsel for Halperin, countered with a claim that when Morgan Stanley bought the company it counted the full amount of its pension liability against the company's value.

"There's no basis for defendants to quibble over the inclusion of the Teamster pension liability," he said.

He also claimed Morgan Stanley withheld information on the pension liabilities from the solvency experts it brought in to look at the company before the 2009 dividend payment and that the pension liabilities caused three other potential buyers to withdraw their offers in 2013.

Morgan Stanley separately argued that because Halperin alleged the funds to pay the dividends came from a bond sale, the dividend payments were protected from clawback under the Bankruptcy Code's "safe harbor" rule for securities transactions, an assertion Judge Drain challenged on multiple grounds.

"I have not seen any argument that the financing for a challenged transaction can serve as the triggering point," he said.

Morgan Stanley and Halerpin also clashed over whether the statute of limitations had run out on the breach of fiduciary duty claims. Morgan Stanley argued Tops Holding was incorporated in Delaware and the Delaware statute of limitations had run out, while Halerpin argued the company conducted all of its business in New York and the longer New York statute of limitations applied.

Judge Drain said he would issue a written ruling on the motions.

Halperin is represented by Kyle A. Lonergan, James H. Smith, Joshua Newcomer, Mike McKool and Lewis T. LeClair of McKool Smith PC.

Morgan Stanley is represented by Pamela A. Miller, Peter Friedman, Daniel S. Shamah and Patrick D. McKegney of O'Melveny & Myers LLP.

The case is Alan D. Halperin v. Morgan Stanley Investment Management Inc. et al., case number 20-08950, in the U.S. Bankruptcy Court for the Southern District of New York.

--Editing by Daniel King.