BEYOND BANKRUPTCY

Court Says Fleming Creditors Can Sue Big Vendor Employees

A bankruptcy judge Wednesday cleared the way for Fleming Cos. creditors to sue specific employees of Dean Foods Co., Kraft Foods Inc., Frito Lay Inc. and other companies that the creditors say had a hand in presenting a false picture of financial health at the defunct grocery wholesaler.

The ruling from U.S. Bankruptcy Judge Mary F. Walrath allows Fleming's creditors to continue moving against employees of some of Fleming's largest suppliers in a federal lawsuit that says vendors helped the wholesaler inflate its books.

At the heart of the action against the Kraft, Dean and Frito-Lay employees are allegations they provided phony papers that helped Fleming fool its auditors and inflate revenue.

Frito-Lay brand products are produced by PepsiCo Inc.

The suppliers have denied wrongdoing, as have the employees. But many of them last year settled Securities and Exchange Commission charges related to their role in the former grocery giant's alleged fraud.

Spokesmen for Dean, Kraft and Frito Lay weren't immediately able to comment on Wednesday's ruling, but lawyers for the vendors said in court that it was unfair to expose their employees to the lawsuits.

The Chapter 11 plan Fleming confirmed in July 2004 set up a mechanism that allows big suppliers to settle their quarrels over Fleming's collapse among themselves.

This, said attorneys for the big suppliers, should also shelter employees, especially because the companies are likely to have to foot the bill if their employees are held liable to Fleming's creditors.

The judge disagreed.

"This means the attempt to prevent innocent creditors from recovering the value of their claims has failed," said Kathy D. Patrick, the Texas lawyer representing the trust set up to gather cash for Fleming's rank-and-file creditors, including bondholders and small suppliers.

In court papers, she said the bid by some of Fleming's biggest vendors to block the lawsuits was an attempt to manipulate the bankruptcy case to shield alleged wrongdoers.

Fleming took cover from creditors in that court in April 2003. In July 2004, the company won confirmation of its Chapter 11 reorganization plan.

The wholesale and retail portions of the business were sold off and only Fleming's convenience store supply business, Core-Mark International Inc., survived the reorganization.

In the wake of Wednesday's ruling, smaller creditors of the one-time wholesaler will be pursuing employees of Fleming's big suppliers in a wide-ranging federal lawsuit in Texas that was started by Fleming shareholders.

Until Wednesday, that case appeared to be drawing to a close.

Shareholders are on their way to a $93.95 million settlement of actions against Fleming's officers and directors, auditor Deloitte & Touche and underwriters accused of complicity in alleged accounting fraud, according to court documents.

While still denying wrongdoing, Deloitte & Touche will pay $35 million to holders. The auditor has already paid an undisclosed amount to Fleming's creditors in a separate settlement.

Underwriters Lehman Brothers Inc., Deutsche Bank Securities Inc., Morgan Stanley & Co. and Wachovia Capital Markets LLC have agreed to pay $27.5 million to Fleming's former shareholders, court documents say.

As part of the pact, Fleming's creditors are receiving $5.5 million from former officers and directors, including five the SEC hit last month with civil securities fraud charges.

Now, however, Fleming's creditors will seek to hold employees of suppliers to account in the lawsuit.

In September 2004, consent decrees with the SEC required suppliers accused of helping Fleming cheat to pay fines ranging from $100,000 to $400,000. Employees were fined from $25,000 to $75,000, without admitting or denying wrongdoing.

In addition to Kraft, Frito-Lay and Deans Foods employees, Fleming's creditors have sued employees of Digital Exchange Systems Inc., Daymon Worldwide Trading Inc., Marigold Foods LLC and Dole Food Co. DBR

—Peg Brickley

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