BOIES, SCHILLER & FLEXNER LLP
575 LEXINGTON AVENUE • 7TH FLOOR • NEW YORK, NY 10022 • PH. 212.446.2300 • FAX 212.446.2350

May 29, 2015

BY HAND

The Honorable Victor Marrero
United States District Court
Southern District of New York
500 Pearl Street
New York, New York 10007

Re: ***Anwar, et al. v. Fairfield Greenwich Limited, et al.***
Master File No. 09-CV-00118 (VM) (FM)

Dear Judge Marrero:

The *Anwar* Plaintiffs respectfully submit this letter memorandum, pursuant to the Court's direction at the telephone conference on April 30, 2015, regarding the application of the Second Circuit's decision in *In re Kingate Management Ltd. Litig.*, 784 F.3d 128 (2d Cir. 2015), to the remaining claims in this action.

INTRODUCTION

This Court decided in *Anwar v. Fairfield Greenwich Ltd.*, 728 F. Supp. 2d 372 (S.D.N.Y. 2010) ("*Anwar II*"), that SLUSA did not bar any of the common law claims brought by Plaintiffs, and that "even if the multiple layers between Plaintiffs investments and the purported purchase of covered securities fell under SLUSA's ambit, only the fraud and negligent misrepresentation common law causes of action would be dismissed." *Id.* at 399 n.7. Now, in light of subsequent decisions of the Supreme Court and the Second Circuit, it is clear that this Court was largely, although not entirely correct: SLUSA's "in connection with" requirement is satisfied by transactions that involve feeder funds, but SLUSA should be interpreted narrowly so as not to bar traditional state law claims absent direct false conduct involving SLUSA-covered securities. Consequently SLUSA does not bar the *Anwar* Plaintiffs' claims for breach of fiduciary duty, breach of contract or negligence-based torts.

As discussed below, under the analytical framework set forth in *Kingate*, SLUSA has no application to the *Anwar* Plaintiffs' duty-based claims asserted against PwC and Citco. "Proof of these claims would not require any showing of *false conduct* on the part of Defendants." *Kingate*, at 152 (emphasis added). Under the *Kingate* framework, "false conduct" is a term of art which means "all the types of misleading or deceptive conduct" prohibited by federal securities

law, "including a misrepresentation or omission of a material fact" concerning a "covered security" as defined in SLUSA. *Id.* at 132. Applying this standard, SLUSA does not bar the *Anwar* Plaintiffs' negligence claim against PwC. *See* Point III.A. Likewise, SLUSA does not preclude the *Anwar* Plaintiffs' duty-based claims against Citco: (i) negligence, (ii) gross negligence, (iii) breach of fiduciary duty, (iv) third party beneficiary breach of contract, and (v) aiding and abetting FGG's breach of fiduciary duty. *See* Point IV.

Further, the negligent misrepresentation claims against PwC and Citco are not precluded because the *Anwar* Plaintiffs do not allege that these Defendants were complicit in Madoff's fraud, but rather that they made misrepresentations and omissions concerning their own conduct and misrepresented the values of "uncovered" securities. *See* Points III.B and IV.E. Only the claim against Citco for aiding and abetting FGG's fraud should be dismissed, as Plaintiffs have already acknowledged.

BACKGROUND

I. The *Anwar* Action

Plaintiffs' Second Consolidated Amended Complaint ("SCAC") asserted federal and state law claims against several sets of defendants. The Court has approved settlements with the Fairfield Greenwich defendants and GlobeOp defendants which dismissed the claims against them. Only the claims against the PwC and Citco defendants remain.

A. Claims Against PwC

From 1994 to 2005, PwC Netherlands served as auditor for the Fairfield Sentry fund, and later the Greenwich Sentry funds, providing clean audit opinions for each of those years. Beginning in 2006, PwC Canada assumed the audit function and similarly provided clean audit opinions for the Funds for 2006 and 2007. The Court in *Anwar II* sustained claims of negligence (Count 13) and negligent misrepresentation (Count 14) against each of the PwC defendants. Count 13 alleges that PwC was negligent in conducting its audits of the Funds' financial statements and these deficient audits caused the *Anwar* plaintiffs to incur substantial losses. Count 14 is premised on audit reports that PwC prepared for the benefit of the Funds' investors. It alleges that PwC negligently misrepresented in its audit reports that PwC had conducted a proper audit in accordance with GAAP or IFRS requirements, and that the Funds' investors relied on these reports in making additional investments as well as holding their existing investments in the Funds.

B. Claims Against Citco

Citco Fund Services (Europe) B.V. and Citco (Canada) Inc. (together, "Citco Administrators") served as administrator for Fairfield Sentry beginning in 1992, for Fairfield Sigma since 1997, and for Greenwich Sentry and Greenwich Sentry Partners since 2006. As administrator, one of Citco's primary duties was to calculate each Fund's net asset value

("NAV"), *i.e.*, the value on a per-share basis of all investments held by the Fund minus its liabilities. Citco Bank Nederland, N.V., Dublin Branch and Citco Global Custody N.V. (together, "Citco Custodians") served as custodian for the Fairfield Sentry and Sigma funds. A fund custodian is responsible for safekeeping of fund assets and settling trades. Citco Group Limited ("Citco Group") is the parent company which closely managed and controlled the subsidiaries.

In *Anwar II*, the Court sustained the following common law claims against Citco:

- Citco Administrators: third-party breach of contract (Count 20), breach of fiduciary duty (Count 21), gross negligence (Count 22), negligence (Count 23), aiding and abetting FGG's breach of fiduciary duty (Count 24) and fraud (Count 25), and negligent misrepresentation (Count 28);

- Citco Custodians: breach of fiduciary duty (Count 21) and aiding and abetting FGG's breach of fiduciary duty (Count 24) and fraud (Count 25);

- Citco Group: gross negligence (Count 22), negligence (Count 23), aiding and abetting FGG's breach of fiduciary duty by FGG (Count 24) and fraud (Count 25), and negligent misrepresentation (Count 28);

- Citco Fund Services Bermuda Ltd. ("Citco Bermuda"): aiding and abetting FGG's breach of fiduciary duty (Count 24) and fraud (Count 25).

Anwar II also upheld federal securities fraud claims against the Citco Administrators and the Citco Group. The federal claims are, of course, not impacted by SLUSA or the *Kingate* decision.

II. SLUSA and How It Has Been Applied

A. SLUSA Must Be Interpreted Narrowly so as Not to Preclude Most Traditional State Law Causes of Action

Anwar II was decided in August 2010; several years later, the Supreme Court decided *Chadbourne & Parke LLP v. Troice*, 134 S. Ct. 1058 (2014). *Troice* involved a Ponzi scheme in which Allen Stanford and his companies falsely represented that uncovered securities (certificates of deposit in Stanford International Bank) that the plaintiffs purchased were backed by covered securities that the bank supposedly was purchasing. The Supreme Court held that SLUSA did not bar the investors' claims: SLUSA does not apply to a class actions in which "the plaintiffs allege (1) that they 'purchase[d]' uncovered securities (certificates of deposit that are not traded on any national exchange), but (2) that the defendants falsely told the victims that the uncovered securities were backed by covered securities." *Troice*, 134 S. Ct. at 1062.

The Supreme Court held that SLUSA "defines 'covered security' narrowly." *Id.* at 1064. Moreover, in interpreting the phrase "in connection with" for purposes of SLUSA, *Troice* held that "a connection matters where the misrepresentation makes a significant difference to someone's decision to purchase or to sell a covered security, **not to purchase or to sell an uncovered security, something about which the Act expresses no concern**." *Id.* at 1066 (emphasis added). "[T]o interpret the necessary statutory 'connection' more broadly than we do here would interfere with state efforts to provide remedies for victims of **ordinary state-law frauds**." *Id.* at 1068 (emphasis added). For instance, the Court found that such a broad interpretation of SLUSA could, incorrectly, "prohibit a lawsuit brought by homeowners against a mortgage broker for lying about the interest rates on their mortgages—if, say, the broker (not the homeowners) later sold the mortgages to a bank which then securitized them in a pool and sold off pieces as 'covered securities.'" *Id.* (citation omitted). In the Supreme Court's example, although third parties who bought covered securities (*i.e.*, the securitized mortgages) would be involved in the chain of events that injured plaintiffs, the Court recognized that interpreting SLUSA broadly to preclude the homeowners' claims would improperly interfere with state law remedies. *Id.*

Accordingly, the Supreme Court rejected "a broad interpretation" of SLUSA that would "work[ ] at cross-purposes" with Congressional intent to preserve appropriate state law claims. *Troice* at 1069. Under *Troice*, "the **only** issuers, investment advisers, or accountants that today's decision will continue to subject to state-law liability are those who don't sell or participate in selling securities traded on U.S. national exchanges" *id.* (emphasis in original) – which is precisely the situation of the PwC and Citco defendants.

Several months before the Supreme Court announced *Troice*, the Second Circuit had decided *In re Herald*, 730 F.3d 112 (2d Cir. 2013) ("*Herald I*"). In *Herald I*, the Court of Appeals applied SLUSA to affirm dismissal of state law claims for aiding and abetting and conspiracy brought by investors in a Madoff feeder fund against JPMorgan and Bank of New York (the "Banks"). These Banks were service providers **solely to Madoff, not to the separate feeder funds**. *Herald I* makes clear that (i) "the proposed plaintiff classes purchased interests that all parties concede are not included within the definition of 'covered security.'" *Id.* at 118. "[R]ather, the plaintiffs' allegations with respect to BNY and JPMorgan relate directly to Madoff's purported transactions in covered securities." *Id.* This conclusion follows from the fact that "the liability of JPMorgan and BNY is **predicated not on these banks' relationship with plaintiffs or their investments in the feeder funds**" – as is the case with respect to the claims against PwC and Citco in *Anwar* – "but on the banks' relationship with, and alleged assistance to, Madoff Securities' Ponzi scheme, which indisputably engaged in purported investments in covered securities on U.S. exchanges." *Id.* at 118-19 (emphasis added).

Of particular significance, the *Herald* plaintiffs also brought claims against the managers, auditors, administrators and custodians of multiple feeder funds based on these defendants' own misstatements and breaches of duty. The *Herald* panel did not dismiss these claims on SLUSA grounds under the reasoning of *Herald I*, but instead wrote a separate, unpublished decision describing these claims involving plaintiffs' purchase of uncovered interests in an offshore hedge

fund as a dispute "over which the United States has no regulatory authority" and dismissed the claims on *forum non conveniens* grounds. *In re Herald*, 540 Fed. App'x 19, 29 (2d Cir. 2013) (summary order); *see also id.* at 27 ("Moreover, although appellants claim that the fact that Madoff Securities' scheme occurred primarily in New York provides a 'bona fide connection to the United States and to [their] forum of choice, . . . **the ties between the claims against these defendants and Madoff's conduct are too tenuous** to require deference to the appellants' choice of forum.") (emphasis added) (citation omitted).

Following *Troice*, the plaintiffs sought rehearing of the *Herald I* decision, but the motion was denied, with the Court of Appeals holding that *Troice* "confirms the logic and holding" of *Herald I*. *In re Herald*, 753 F.3d 110, 113 (2d Cir. 2014) ("*Herald II*"). As in the original decision, *Herald II* found that SLUSA applied because "Madoff Securities . . . fraudulently induced attempted investments in covered securities, albeit through feeder funds (not alleged in the instant complaints as anything other than intermediaries), and the defendant banks are alleged to have furthered that scheme." *Id.*

B. The *Kingate* Framework

In the *Kingate* decision on April 23, 2015, the Second Circuit vacated Judge Batts' decision to dismiss common law claims asserted in an investor class action against defendants who promoted, managed, audited and administered the Kingate feeder fund. *See In re Kingate Mgmt. Ltd. Litig.*, 784 F.3d 128 (2d Cir. 2015). Applying *Herald*, the Court of Appeals "conclude[d] that the alleged fraud in [*Kingate*] is 'in connection with the purchase or sale of a covered security' and thus qualifies to bring the case within SLUSA's prohibition (assuming SLUSA's other necessary elements are met)." *Id.* at 132 (citing 15 U.S.C. § 78bb(f)(1)). The Court then went on to consider SLUSA's application to "the numerous distinct state law theories of liability asserted" in *Kingate* and held that "state law claims that do not depend on false conduct are not within the scope of SLUSA, even if the complaint includes peripheral, inessential mentions of false conduct; and ii) claims accusing the defendant of complicity in the false conduct that gives rise to liability are subject to SLUSA's prohibition, while claims of false conduct in which the defendant is not alleged to have had any complicity are not." *Kingate*, at 132.

To address the various causes of actions and distinct theories of liability against several different groups of defendants in *Kingate*, the Court of Appeals divided the allegations "into five groups for purposes of analyzing SLUSA's application, with the understanding that certain counts of the Complaint may include allegations from more than one of these groups." *Id.* at 134. The five groups articulated by the Second Circuit were:

1. Group 1 consists of those allegations that predicate the named Defendants' liability on their own fraudulent misrepresentations and misleading omissions (i.e., those made with scienter), made in connection with the Funds' investments with Madoff in covered securities and with their oversight of these investments.

2. The allegations of Group 2 are similar to Group 1, with the exception that liability is premised on the named Defendants' *negligent* misrepresentations and omissions, rather than intentional misrepresentations and omissions.

3. The Group 3 allegations predicate liability on Defendants' aiding and abetting (rather than directly engaging in) the frauds underlying the Group 1 claims.FN.6

4. The allegations of Group 4 predicate liability on Defendants' breach of contractual, fiduciary, or tort-based duties owed to Plaintiffs, resulting in failure to detect the frauds of Madoff and BMIS.

5. The allegations of Group 5 seek compensation for fees paid to the named Defendants by the Funds on the grounds that those Defendants failed to perform the duties for which the fees were paid, or that the fees based on purported profits and values of the Funds were computed on the basis of inaccurate values.[1]

Id. at 134-35.

The *Kingate* decision directed that application of SLUSA must be analyzed on a claim-by-claim basis and that, even within a particular claim, the court must identify which allegations are "necessary" to the claim, and those that are "inessential" or "extraneous." *Id.* at 132, 142. "[S]tate law claims that do not **depend** on false conduct are not within the scope of SLUSA." *Id.* at 132 (emphasis in original). A cause of action may be covered by SLUSA only if it alleges conduct on the part of the defendant that amounts to a fraud involving covered securities. "Only conduct by the defendant is sufficient to preclude an otherwise covered class action." *Id.* "[C]onstruing 'alleging' as applying where the false conduct alleged (in connection with a transaction in a covered security) is essential to the success of the state law claim, but is not conduct of the defendant, would result in barring numerous suits that were altogether outside of Congress's purposes in passing SLUSA . . . ." *Id.* at 147-48. On the other hand, a claim is precluded if the success of that claim "depends on a showing that the **defendant committed false conduct conforming to SLUSA's specifications**." *Id.* at 149 (emphasis added).

---

[1] The Second Circuit further stated: "The allegations falling in Groups 3, 4, and 5 do not include allegations proof of which depends on a showing that the named Defendants committed knowing, intentional, or negligent misrepresentations or misleading omissions in connection with transactions in covered securities. If allegations that otherwise fit within the description of Group 3, 4, or 5, require proof that the Defendants committed such misrepresentations, then those allegations belong in Group 1 or 2 rather than in Group 3, 4, or 5." *Id.* at 135 n.6. The Court also stated "that plaintiffs should not be permitted to escape SLUSA by artfully characterizing a claim as dependent on a theory other than falsity when falsity nonetheless is essential to the claim, such as by characterizing a claim of falsity as a breach of the contractual duty of fair dealing." *Id.* at 140.

The Second Circuit went on to emphasize that "[i]f, for example, we are told that X has been charged with 'allegations of fraud,' or that X is named as a defendant in a suit 'alleging fraud,' we understand this to mean that X is accused of having committed fraud, and not that he is charged with negligence or breach of contract in failing to detect someone else's fraud . . . ." *Id.* at 147. To illustrate the distinction, the Court gave examples of conduct that would not be barred by SLUSA. *Id.* at 147-48. The first illustrative example involved claims by the clients of a dishonest stockbroker who bring a negligence action against an accounting firm which they hired to audit their brokerage accounts. Because the auditor's examination of the accounts was negligent, it failed to detect the fraud. "It is true that the negligence claim includes an allegation of fraud in connection with transactions in covered securities and that the alleged fraud by the broker is an essential predicate of the plaintiffs' claims against the defendant auditor. However, the auditor is not alleged to have committed any of the conduct specified in SLUSA." *Id.* at 148. Accordingly, a suit against the auditor based on the negligent audit falls outside the scope of SLUSA. *Id.* Other than the fact that the brokerage clients in the Second Circuit's example hired the auditor (a fact which has nothing to do with application of SLUSA), this example is on all fours with the claims in *Anwar* against PwC (and against Citco with respect to provision of analogous non-audit services).

In applying this framework to the plaintiffs' claims in *Kingate*, the Second Circuit found that "the allegations described in Group 1. . . predicate liability on charges that Defendants fraudulently made misrepresentations and misleading omissions regarding the Funds' investments with Madoff and their oversight of the Funds' investments. Under *Herald,* these claims allege falsity 'in connection with' covered securities." *Id.* at 151. Additionally, the claims "allege conduct by Defendants falling within SLUSA's specifications of conduct prohibited by the anti-falsity provisions of the 1933 and 1934 Acts. Accordingly, SLUSA precludes Plaintiffs' Group 1 allegations." *Id.* The Court of Appeals found that the allegations in Group 2 also were precluded because they alleged similar misstatements and omissions involving covered securities and only "differ from those in Group 1 in that they charge the Defendants with negligent misrepresentations (i.e., without scienter) rather than fraudulent misrepresentations." *Id.* "The allegations described in Group 3 charge that Defendants aided and abetted (rather than directly committed) the frauds described in Group 1. *Herald* ruled that such allegations are precluded by SLUSA." *Id.*

The Second Circuit then considered the allegations described in Group 4. It found that "[t]hese predicate liability on Defendants' breach of contractual, fiduciary, and/or tort-based duties to Plaintiffs to provide competent management, consulting, auditing, or administrative services to the Funds, thus allowing Madoff's frauds to go undetected, causing Plaintiffs' losses." The Court of Appeals concluded "that such allegations are not precluded by SLUSA" based on the following reasoning:

> [A]s defined above, allegations within Group 4 do not include those requiring a showing of false conduct **by the named Defendants** of the sort specified in SLUSA. The only false conduct involved in the Group 4 allegations is that of Madoff and BMIS. Under the Group 4 theories of liability, Defendants, like

> Plaintiffs, were victims of Madoff's frauds. The asserted liability of Defendants under these claims arises from the fact that Defendants breached their contractual and duty-based obligations to Plaintiffs. Proof of these claims would not require any showing of false conduct on the part of Defendants.

Id. at 151-52 (emphasis in original).

ARGUMENT

The remaining common law claims against PwC and Citco asserted in *Anwar* fall squarely into Group 4 and, therefore, are not barred by SLUSA, with the exception of Count 25 against Citco, which alleges aiding and abetting fraud by the Fairfield Defendants. The Second Circuit held that "[t]he Group 4 allegations differ crucially from those found in *Herald* to be precluded by SLUSA." *Id.* at 152 n.23 (citing *Herald I,* 730 F.3d at 119 n. 7). "The *Herald* claims asserted liability based on defendants' alleged **complicity in Madoff's fraudulent scheme**. *See id.* Only Groups 1, 2, and 3 allege Defendants to have been, in varying degrees, **complicit in the falsity**." *Id.* (emphasis added). In Plaintiffs' claims in *Anwar*, PwC and Citco are not alleged to have been complicit in Madoff's fraud. Instead, liability arises from the fact that PwC and Citco breached duties owed directly to Plaintiffs as investors in the Fairfield Funds. Moreover, the negligent misrepresentation claims against PwC and Citco are not based on the type of allegations that fall into Group 1, which require allegations of misrepresentations or omissions "regarding the Funds' investments with Madoff" and "oversight of the Funds' investments." *Id.* at 151. By contrast, the claims against PwC and Citco here allege that these defendants negligently misrepresented that they themselves were "provid[ing] competent . . . auditing or administrative services to the Funds, thus allowing Madoff's frauds to go undetected, causing Plaintiffs' losses." *Id.* Accordingly, these are likewise Group 4 claims which are not precluded.

III. Common Law Claims against PwC Are Not Precluded

A. Negligence

The *Kingate* decision makes clear that negligence by auditors in failing to detect a fraud involving covered securities is a textbook Group 4 claim which is not barred by SLUSA. *See Kingate*, 784 F.3d at 147-52. The negligence claim against PwC is similar to the first illustrative example provided in the *Kingate* opinion and falls into the Second Circuit's description of Group 4 claims. *Id.*

A negligence claim must allege "(1) that the defendant owed him or her a cognizable duty of care; (2) that the defendant breached that duty; and (3) that the plaintiff suffered damage as a proximate result of that breach." *Di Benedetto v. Pan Am World Serv., Inc.*, 359 F.3d 627, 630 (2d Cir. 2004); *see Anwar II*, at 432. The SCAC alleges "PwC, as the Funds' auditors, had a special relationship with Plaintiffs that gave rise to a duty to exercise due care." SCAC ¶ 434. It further alleges that "PwC negligently failed to exercise due care by failing to properly audit the Funds in accordance with GAAS and other applicable auditing standards and thereby caused

injury to the Plaintiffs, who have lost all, or substantially all, of their investments in the Funds." SCAC ¶ 437. The *Kingate* decision expressly recognizes that Madoff's role in the causative chain does not bring the claim within SLUSA's ambit. *Kingate*, 784 F.3d at 147 ("we understand this to mean that X is accused of having committed fraud, and not that he is charged with negligence or breach of contract in failing to detect someone else's fraud"). There is no need to plead or prove any misstatement at all, let alone a misstatement about a SLUSA-covered security.

As mentioned, the negligence claim against PwC fits squarely into one of the examples set forth in the *Kingate* opinion as a claim not barred by SLUSA:

> As a first example, assume the plaintiffs, who are clients of a stockbroker, engaged an auditor to audit their accounts. The auditor examines the accounts of the plaintiffs' securities transactions, does so negligently, and finds everything in order. Later it emerges that the broker had committed frauds against the plaintiffs and that the auditor's negligent examination failed to uncover the frauds. The plaintiffs sue the auditor in a state-law class action, alleging negligence in failing to detect the stockbroker's frauds. It is true that the negligence claim includes an allegation of fraud in connection with transactions in covered securities and that the alleged fraud by the broker is an essential predicate of the plaintiffs' claims against the defendant auditor. However, the auditor is not alleged to have committed any of the conduct specified in SLUSA. The plaintiffs' claim, if brought in federal court under diversity or supplemental jurisdiction, would not be subject to the restrictions of the PSLRA because it would not charge the defendant with a violation of the securities acts. Such a suit appears to us to be outside the concerns of the federal securities laws, the PSLRA, and SLUSA.

Kingate, at 148.

Accordingly, the negligence claim against PwC is a Group 4 claim which is not precluded because proof of this claim "would not require any showing of false conduct on the part of [PwC]." *Id.*, at 152.

B. Negligent Misrepresentation

The negligent misrepresentation claim against PwC is likewise not precluded. Although certain negligent misrepresentation claims fall within Group 2, not all negligent misrepresentation claims are barred. *Kingate*'s discussion of Group 1 claims makes clear that SLUSA does not simply bar **any** misrepresentation – but only "fraudulent misrepresentations and misleading omissions . . . made in connection with the Funds' investments with Madoff in covered securities and with their oversight of these investments." *Kingate*, at 134. Group 2 claims must involve the same type of misrepresentations and omissions, except without scienter. *See id.* at 135.

In contrast, the negligent misrepresentation claim against PwC is based on statements in PwC's audit reports "falsely representing to plaintiffs that (i) [PwC] had conducted its audits in accordance with GAAS or ISA and (ii) the Funds' financial statements presented fairly, in all material respects the financial condition of the Funds." SCAC ¶ 440. These are statements that relate to (i) PwC's own conduct, and (ii) the accuracy of the Funds' financial statements which PwC said contained no material misrepresentations. These misstatements by PwC said nothing about Madoff or his purported trading in covered securities. Nor do the misrepresentations in PwC's one-page audit letters make any mention of Madoff or covered securities. *See, e.g.*, Exhibit 1. The only "essential" allegation related to PwC's misrepresentation is the false statement in the audit report, addressed to the Funds' shareholders, that "[PwC] conducted our audit of these financial statements in accordance with auditing standards generally accepted in the United States of America." *Id.* And one of PwC's principal defenses has been to argue that it was retained solely to audit the Fairfield Funds and had no obligation to audit Madoff: "The 42 defendants [named in the SCAC] do not include Madoff or his firm but do include PwC Netherlands, which never audited Madoff or his business and which is not alleged to have known of or to have participated in Madoff's scheme." Memo in Support of PwC Netherlands Motion to Dismiss, Dkt. No. 317 at 1 (S.D.N.Y. Dec. 22, 2009).

Plaintiffs' claims against PwC do not rest on any allegation that PwC was complicit in Madoff's fraud involving covered securities. Instead, the liability is based on PwC's failure to conduct proper audits. Likewise, the negligent misrepresentation claim is based on PwC's statement that it conducted audits in compliance with the relevant standards, which plaintiffs will demonstrate is false. Accordingly, this claim arises out of the type of "tort-based duties to Plaintiffs to provide competent . . . auditing . . . services to the Funds, thus allowing Madoff's frauds to go undetected, causing Plaintiffs' losses," which falls into Group 4. *Kingate*, at 151.

IV. Common Law Claims Against Citco Are Not Precluded

A. Third Party Beneficiary Breach of Contract

Count 20 arises from the alleged breach of contractual duties that the Citco Administrators owed to Plaintiffs. In ruling on the motions to dismiss, this Court held that Plaintiffs adequately alleged that they were third-party beneficiaries of Citco's administration contacts with the Funds. Citco's duties included, *inter alia*, the following:

> "reconciliation of cash and other balances at brokers"; "reconciliation of bank accounts"; "calculation of income and expense accruals"; "calculation of management and performance/performance fees with supporting schedules"; "independent reconciliation of the Fund's portfolio holdings"; "calculation of the Net Asset Value and the Net Asset Value per Share on a monthly basis in accordance with the Fund Documents"; "Preparation of monthly financial statements, in conformity with the International Accounting Standards," including "Statement of Assets and Liabilities," "Statement of Operations," "Statement of Changes in Net Assets," "Statement of Cash Flows," and "Portfolio listings";

> "Preparation of books and records (including specific schedules and analysis) to facilitate external audit, and liaising with the Fund's auditors in their review and preparation of the annual financial statements"; "Provision of accounting or accounting related reports and/or support schedules as agreed between the Administrator and the Investment Manager"; and "Disbursement of payments for third party fees and expenses incurred by the Fund."

SCAC ¶ 476. To establish this claim, there is no need to prove that Citco made any false statements and, therefore, the claim falls into Group 4. All that is "essential" to this claim is a showing that Citco breached one or more of its many duties owed to investors and that Plaintiffs suffered damages as a result. *See, e.g., LNC Investments, Inc. v. First Fid. Bank, N.A. New Jersey*, 173 F.3d 454, 461 (2d Cir. 1999); *Anwar II*, at 418.

Furthermore, the Second Circuit in describing Group 4 claims expressly stated that the "asserted liability of Defendants under these claims arises from the fact that Defendants breached their contractual . . . obligations to Plaintiffs." *Kingate*, at 152. The Court's example of a contract-based claim not subject to preclusion involved a custodian, *see id.* at 148-49, but the analysis is the same for contractual duties of an administrator.

B. Breach of Fiduciary Duty

Count 21 asserts claims for breach of fiduciary duty against the Citco Administrators and the Citco Custodians. "The elements of a claim for breach of a fiduciary obligation are: (i) the existence of a fiduciary duty; (ii) a knowing breach of that duty; and (iii) damages resulting therefrom." *Johnson v. Nextel Comm'ns, Inc.*, 660 F.3d 131, 138 (2d Cir. 2011); *see Anwar II*, at 415, 440-42.

The Citco Administrators "breached their fiduciary duties to Plaintiffs, by among other omissions, failing to discharge properly their responsibilities as Administrators and Sub-Administrators, including calculating the Funds' NAV and communicating fictitious valuations to Plaintiffs." SCAC ¶ 495. The breach of fiduciary duty claim against the Citco Custodians is based on allegations that these defendants "breached their fiduciary duties by, among other omissions, failing to discharge properly their responsibilities as Custodian and Bank, sub-delegating responsibilities to BMIS without adequate supervision or control, failing to supervise or monitor BMIS as a sub-custodian, and handing over Plaintiffs' investments to BMIS." SCAC ¶ 496. Both the Citco Administrators and Citco Custodians failed to follow industry-standard procedures in performing services for the Funds and investors and they failed to properly follow up on grave concerns raised by internal auditors. Count 21 falls into Group 4 because it "would not require any showing of false conduct on the part of [the Citco Administrators or Citco Custodians]." *Kingate*, at 152. The Court of Appeals expressly identified breach of fiduciary duty as a non-precluded Group 4 claim and, as noted above, gave as an example of such a non-precluded duty-based cause of action a claim against a custodian. *See id.* at 148-49.

C. Gross Negligence and Negligence

Plaintiffs' claims of gross negligence (Count 22) and negligence (Count 23) against the Citco Administrators and the Citco Group are Group 4 claims not barred by SLUSA. "These [claims] predicate liability on [Citco's] breach of . . . tort-based duties to Plaintiffs to provide competent . . . administrative services," which *Kingate* characterized as Group 4 claims. *Kingate*, at 151. As discussed above, a negligence (and a gross negligence) claim does not require any false representation. The crux of these claims is that Citco grossly or negligently "failed to exercise due care and failed to exercise the degree of prudence, caution, and good business practice that would be expected of any reasonable investment professional." SCAC ¶¶ 503, 507. As such, "[t]he asserted liability of [Citco] under these claims arises from the fact that [Citco] breached their . . . duty-based obligations to Plaintiffs. Proof of these claims would not require any showing of false conduct on the part of Defendants." *Kingate*, at 152. Therefore, "such allegations are not precluded by SLUSA." *Id.* In describing Group 4 claims, the Second Circuit in *Kingate* expressly referenced to negligence by "administrators" in performing their duties as a claim that is not precluded. *Id.* at 151.

D. Aiding and Abetting FGG's Breach of Fiduciary Duty

The aiding and abetting breach of fiduciary duty claims (Count 24) against the Citco Administrators, Citco Custodians, the Citco Group and Citco Bermuda also are not barred by SLUSA. "To state a claim for aiding and abetting a breach of fiduciary duty, a plaintiff must show: '(1) breach of fiduciary obligations to another of which the aider and abettor had actual knowledge; (2) the defendant knowingly induced or participated in the breach; and (3) plaintiff suffered actual damages as a result of the breach.'" *Anwar II*, 728 F. Supp. 2d at 442 (quoting *Kottler v. Deutsche Bank AG,* 607 F. Supp. 2d 447, 466 (S.D.N.Y. 2009)).

Here, Citco was aware that FGG owed a fiduciary duty to Plaintiffs; Citco also was aware that FGG's due diligence and risk controls were grossly deficient; and Citco substantially assisted FGG in those breaches by "receiving investments from Plaintiffs and transferring their investments directly to BMIS; calculating the Funds' NAV and disseminating the NAV values; receiving and transmitting other Fund information from the Fairfield Defendants to Plaintiffs; and allowing Citco's name to be used." SCAC ¶¶ 512-13. The "essential" elements of this claim do not include any misrepresentation and liability flows from Citco's awareness of FGG's failure to conduct proper due diligence and institute adequate risk controls. And as noted above, a breach of fiduciary duty claim itself is generally a Group 4 claim that is not precluded.

E. Negligent Misrepresentation

The negligent misrepresentation claims against the Citco Administrators and the Citco Group (Count 28) are not barred by SLUSA. This claim is based on Citco's "false NAV and account balance statements for the Funds." SCAC ¶ 534. The false statements that Citco made about the Funds' NAVs are representations made by Citco about the value of the Funds, which are indisputably not covered securities. Citco's NAV statements make no mention of Madoff or

covered securities; they simply set forth a dollar (or Euro) amount of the purported NAV for each Fund that was false because it overstated the Fund's value by more than 1900%. In addition, the Court has held that this claim can proceed on the basis of Citco's omissions regarding its own negligent conduct in failing to adhere to its own procedures for calculating NAVs and to industry-standard procedures for performing administrative services. *See Anwar v. Fairfield Greenwich Ltd.*, 2015 WL 935454, at *13 (S.D.N.Y. Mar. 3, 2015).

Moreover, Citco's duty to provide Plaintiffs with accurate information regarding the Funds "is predicated" on Citco's "relationship with plaintiffs [and] their investments in the feeder funds," which are not covered securities. *Herald I*, 730 F.3d at 118-19. In contrast, the precluded claims in *Herald I* against JPMorgan and Bank of New York arose out of "the banks' relationship with, and alleged assistance to, Madoff Securities' Ponzi scheme, which indisputably engaged in purported investments in covered securities on U.S. exchanges." *Id.* Accordingly, the allegations supporting the negligent misrepresentation claims against Citco "differ crucially from those found in *Herald* to be precluded by SLUSA" because those claims "asserted liability based on defendants' alleged complicity in Madoff's fraudulent scheme." *Kingate*, at 152 n.23. The negligent misrepresentation claim, like all claims against Citco, does not allege that Citco was complicit in Madoff's fraud – but rather alleges that Citco is liable for its own misconduct in issuing false NAVs and omitting information about Citco's own conduct. It follows that the negligent misrepresentation claim is a Group 4 claim which is not precluded.

F. Aiding and Abetting FGG's Fraud

Plaintiffs acknowledge that Count 25 should be dismissed as a Group 3 claim because FGG's fraud involved false representations about Madoff's purported investments in covered securities and FGG's oversight over Madoff. *See, e.g.*, SCAC ¶¶ 184-86, 193, 234-35.

CONCLUSION

For the foregoing reasons, SLUSA preclusion does not apply to any of Plaintiffs' remaining common law claims against the PwC Defendants and the Citco Defendants, other than Count 25. Plaintiffs respectfully request that the Court reaffirm its rulings in *Anwar II* as to the inapplicability of SLUSA to these claims and proceed to trial in accordance with the recently-ordered schedule.[2]

Respectfully yours,

David A. Barrett

cc: All counsel in *Anwar* and *Standard Chartered* cases (by e-mail)

The Clerk of Court is directed to enter into the public record of this action the letter above submitted to the Court by the Anwar Plaintiffs.

SO ORDERED.

6-4-15
DATE

VICTOR MARRERO, U.S.D.J.

[2] SLUSA "by its terms only affects claims based upon the laws of a state or territory of the United States." *LaSala v. Bordier et Cie*, 519 F.3d 121, 143 (3d Cir. 2008) (SLUSA does not bar claims asserted under Swiss law). Accordingly, if the Court were to find that a claim is precluded, Plaintiffs should be permitted to replead the claim, under foreign law by demonstrating that "(1) a foreign country has the most significant interest in having its law apply (the traditional choice-of-law test), and (2) the United States is the most appropriate forum (the traditional forum-non-conveniens test)." *Id.*

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Chartered Accountants
PO Box 82
Royal Trust Tower, Suite 3000
Toronto Dominion Centre
Toronto, Ontario
Canada M5K 1G8
Telephone +1 416 863 1133
Facsimile +1 416 365 8215

April 7, 2008

Report of Independent Auditors

To the Directors and Shareholders of
Fairfield Sentry Limited

In our opinion, the accompanying balance sheet and the related income statement, the statement of changes in net assets attributable to holders of redeemable participating shares and the cash flow statement present fairly, in all material respects, the financial position of **Fairfield Sentry Limited** (the "Company") as of December 31, 2007 and the results of its operations, the changes in its net assets attributable to holders of redeemable participating shares and its cash flows for the year then ended in conformity with International Financial Reporting Standards. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these financial statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by the Company's management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Chartered Accountants, Licensed Public Accountants

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers Accountants N.V.
Fascinatio Boulevard 350
3065 WB Rotterdam
P.O. Box 8800
3009 AV Rotterdam
The Netherlands
Telephone +31 (10) 407 55 00
Facsimile +31 (10) 456 43 33
www.pwc.com/nl

To the directors and shareholders of
Fairfield Sentry Limited

Auditors' report

Introduction

In accordance with your assignment we have audited the accompanying balance sheet of Fairfield Sentry Limited ('the Company') as at December 31, 2005 and the related statements of income, changes in net assets attributable to holders of redeemable participating shares and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

Scope

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion the financial statements give a true and fair view of the financial position of the Company as at December 31, 2005 and of the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Rotterdam, June 26, 2006

PricewaterhouseCoopers Accountants N.V.

H.F.M. Gertsen RA

FG-1411u-av-00428220001