UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK
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ANWAR, et al.,

Plaintiffs,

-against-

FAIRFIELD GREENWICH LIMITED, et al.,

Defendants.

MASTER FILE NO.
09-CV-0118 (VM)

This Document Relates To: All Actions
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REPLY MEMORANDUM IN SUPPORT OF DEFENDANTS IAN PILGRIM AND CITCO FUND SERVICES (BERMUDA) LIMITED'S MOTION TO DISMISS THE SECOND CONSOLIDATED AMENDED COMPLAINT

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INTRODUCTION

Plaintiffs' Opposition[1] makes clear that the only claim against Pilgrim is for breach of fiduciary duty, and the only claims against CFSB are based on theories of *respondeat superior* and agency.[2] What is also clear is that the claim against Pilgrim fails because (i) Pilgrim owed no fiduciary duty to Plaintiffs, who were shareholders of a separate company than the one for which Pilgrim served as a director; (ii) any claim for breach of fiduciary duty would be derivative; and (iii) any such claim would be time-barred. Plaintiffs' Opposition makes equally clear that the *respondeat superior* claim against CFSB fails because its employees, Pilgrim and Francoeur, were not acting as CFSB's agents and have no liability in any event.[3] Similarly, the agency-based claims against CFSB fail because the SCAC does not state a claim against any of CFSB's affiliates, and also does not establish that any of them acted as CFSB's agents. For these reasons, the claims against Pilgrim and CFSB should be dismissed with prejudice.

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[1] "Plaintiffs' Opposition" or "Pl. Opp." refers to Plaintiffs' Memorandum in Opposition to Motions to Dismiss by the Citco Defendants, Pilgrim and Francoeur (D.E. 420). "Opening Memorandum" refers to the Memorandum of Law in Support of Defendants Ian Pilgrim and Citco Fund Services (Bermuda) Limited's Motion to Dismiss the Second Consolidated Amended Complaint (D.E. 336). "FGG's Opening Memorandum" refers to the Memorandum of Law in Support of the Motion to Dismiss the Second Consolidated Amended Complaint on Behalf of the FGG Defendants (D.E. 364). "Plaintiffs' Opposition (FGG)" refers to Plaintiffs' Consolidated Opposition to the Fairfield Greenwich Defendants' Motions to Dismiss (D.E. 418).

[2] Plaintiffs have abandoned their unjust enrichment claim against Pilgrim and CFSB (Count 33) given that they have not responded to the arguments in the Opening Memorandum. *See Burchette v. Abercrombie & Fitch Stores, Inc.*, No. 08 Civ. 8786 (RMB)(THK), 2009 WL 856682, at *8-9 (S.D.N.Y. Mar. 30, 2009).

[3] CFSB incorporates by reference Francoeur's Reply Memorandum.

ARGUMENT

I. The Breach of Fiduciary Duty Claim Against Pilgrim Should Be Dismissed

A. Pilgrim Did Not Owe Plaintiffs a Fiduciary Duty

Plaintiffs have sued Pilgrim based on his role as a director of FGBL, a Bermuda corporation. Under the internal affairs doctrine, claims alleging that FGBL's directors breached their fiduciary duties are governed by Bermuda law. *See, e.g., BBS Norwalk One, Inc. v. Raccolta, Inc.*, 60 F. Supp. 2d 123, 129 (S.D.N.Y. 1999) ("Under New York law, issues relating to the internal affairs of a corporation are decided in accordance with the law of the state of incorporation."), *aff'd*, 205 F.3d 1321 (2d Cir. 2000). Under Bermuda law, a director owes a fiduciary duty only to the company on whose board the director sits. (*See* Affidavit of Rod S. Attride-Sterling (D.E. 362, at ¶ 13).) A director owes no fiduciary duty to the individual shareholders of that company or, as Plaintiffs claim here, to shareholders of a separate company. *Id.* Having failed to refute Mr. Attride-Sterling's affidavit in their Opposition, Plaintiffs have conceded that their breach of fiduciary duty claim cannot be sustained as a matter of Bermuda law. Thus, Plaintiffs' breach of fiduciary duty claim should be dismissed.[4]

[4] While Plaintiffs argue that New York law should be applied to their fiduciary duty claim, the failure to allege that Pilgrim committed a tort, or made a misrepresentation to Plaintiffs, in New York renders the cases Plaintiffs offer in support of this argument wholly inapplicable. For example, in *Roselink Investors, L.L.C. v. Shenkman*, 386 F. Supp. 2d 209, 215 (S.D.N.Y. 2004), the court did, in fact, apply the law of the state of incorporation to the breach of fiduciary claim. Other cases Plaintiffs rely on are inapposite because they involved claims that the defendants made misrepresentations that induced plaintiffs to make investments. *See PPI Enters. (U.S.), Inc. v. Del Monte Foods Co.*, No. 99 Civ. 3794 (BSJ), 2003 WL 22118977, at *17-18 (S.D.N.Y. Sept. 11, 2003); *Pension Comm. of the Univ. of Montreal Pension Plan v. Banc of Am. Sec., LLC*, 446 F. Supp. 2d 163, 194-95 (S.D.N.Y. 2006); *cf. Koury v. Xcellence, Inc.*, 649 F. Supp. 2d 127, 138-39 (S.D.N.Y. 2009) (distinguishing *Pension Committee* and applying the internal affairs doctrine to breach of fiduciary duty claim). Also inapplicable are *Stephens v. National Distillers and Chemical Corp.*, Nos. 91 Civ. 2901 (JSM) and 91 Civ. 2902 (JSM), 1996 WL 271789, at *4-5 (S.D.N.Y. May 21, 1996) (applying New York law because foreign insurer doing business in New York was subject to New York statutes governing insurer's obligations

Even if this Court were to apply New York law, Plaintiffs' breach of fiduciary duty claim still fails. Contrary to Plaintiffs' argument (Pl. Opp. at 22-23), Pilgrim's mere status as a director of FGBL does not impose on Pilgrim a fiduciary duty owed to the shareholders of separate companies (*i.e.*, Fairfield Sentry and Fairfield Sigma). Under New York law, "[a] corporate officer or director generally owes a fiduciary duty ***only*** to the corporation over which he exercises management authority." *Bank of Am. Corp. v. Lemgruber*, 385 F. Supp. 2d 200, 224 (S.D.N.Y. 2005) (emphasis added).[5] Plaintiffs cite no authority refuting this rule of law, nor do they cite any other authority suggesting a basis by which Pilgrim, as a result of his status as a director of FGBL, owed a fiduciary duty to Plaintiffs, who were shareholders of entirely separate companies.[6]

Plaintiffs' attempts to distinguish the cases relied upon by Pilgrim are also unavailing. While Plaintiffs contend that *A.I.A. Holdings, S.A. v. Lehman Brothers, Inc.*, No. 97 Civ. 4978 (LMM), 1999 WL 47223, at *6 (S.D.N.Y. Feb. 3, 1999), was decided in the context of a fraud by a broker, they conveniently ignore the fact that the court held that the defendant's status as a 50% shareholder, officer and director of the fund did not create a fiduciary relationship with the investors of the fund. *Id.* Similarly, in *Renner v. Chase Manhattan Bank*, No. 98 Civ. 926

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and duties), and *In re Adelphia Communications Corp.*, 365 B.R. 24, 31, 39-41 (Bankr. S.D.N.Y. 2007) (applying New York law to aiding and abetting breach of fiduciary duty claims against directors), *aff'd in part sub nom. Adelphia Recovery Trust v. Bank of America, N.A.*, 390 B.R. 64 (S.D.N.Y. 2008).

[5] Plaintiffs' reliance on *Bullmore v. Banc of America Securities LLC*, 485 F. Supp. 2d 464, 470 (S.D.N.Y. 2007), is misplaced. The public policy analysis in *Bullmore* expressly depended on relationships traditionally deemed to be fiduciary in nature, such as attorney-client and general partner-limited partner. Plaintiffs have alleged no such relationship here.

[6] Beyond the conclusory allegation that, as a director, Pilgrim "had responsibility for FGBL" (Pl. Opp. at 22), Plaintiffs fail to allege any facts suggesting that Pilgrim was anything more than an outside director of FGBL, or that Pilgrim was in any way involved in the day-to-day operations of FGBL.

(CSH), 2000 WL 781081, at *20 (S.D.N.Y. June 16, 2000), *aff'd*, 85 F. App'x 782 (2d Cir. 2004), the court found that the defendant, which had contracted to facilitate transactions of the funds on behalf of the funds' clients, could not be held liable for a breach of fiduciary duty when it did not accept any entrustment of confidence or have any meaningful contact with the funds' clients. *Id.* As these cases demonstrate, a director of a company cannot be held liable to the shareholders of a separate entity for breach of fiduciary duty based solely on his status as a director.[7] *See Rotter v. Institutional Brokerage Corp.*, No. 93 Civ. 3578 (JFK), 1994 WL 389083, at *4 (S.D.N.Y. July 22, 1994) ("directors or officers of a corporation do not incur personal liability for torts of a corporation, such as a breach of fiduciary duty, solely because of their positions as directors and officers").

Further, Plaintiffs do not allege a single instance of contact or communication between Pilgrim and any Plaintiff, and thus Plaintiffs cannot come close to demonstrating that they "reposed trust and confidence" in Pilgrim or that Pilgrim accepted that trust, as is required to establish a fiduciary relationship. *See Thermal Imaging, Inc. v. Sandgrain Sec., Inc.*, 158 F. Supp. 2d 335, 343-44 (S.D.N.Y. 2001). For that reason, the cases relied upon by Plaintiffs (Pl. Opp. at 23) are inapposite. For example, unlike Plaintiffs here, the plaintiff in *Crossen v. Bernstein*, No. 91 Civ. 3501 (PKL), 1994 WL 281881 (S.D.N.Y. June 23, 1994), specifically alleged that the defendants made numerous fraudulent misrepresentations in order to induce him to make investments, and that all of the defendants were known by the plaintiff to be attorneys and accountants in whom the plaintiff had reposed trust and confidence. *Id.* at *1, 4.

[7] Even if the Court were to apply New York law to Plaintiffs' breach of fiduciary duty claim against Pilgrim, that claim is preempted by New York's Martin Act. *See* CBN/CGC's Reply Memorandum at pages 7-10; *see also Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 190 (2d Cir. 2001); *Stephenson v. Citco Group Limited*, No. 09 CV 00716 (RJH), 2010 WL 1244007, at *13-15 (S.D.N.Y. April 1, 2010).

Significantly, the court dismissed the breach of fiduciary duty claim because it was derivative and belonged to the limited partnership, while allowing the fraudulent concealment claim to be brought directly because it was based on the allegations of misrepresentation. *Id.* at *3-4. Similarly, in *Tobias v. First City National Bank and Trust Co.*, 709 F. Supp. 1266, 1278 (S.D.N.Y. 1989), the court allowed a breach of fiduciary duty claim against a director of the general partner precisely because the director allegedly made misrepresentations to the plaintiffs designed to induce them to purchase an interest in the limited partnership.[8]

B. The SCAC Fails to Allege a Breach of Fiduciary Duty

Even if a fiduciary duty was owed by Pilgrim to Plaintiffs, the SCAC's conclusory allegations are insufficient to establish a breach of that duty. (Pl. Opp. at 24.) *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555-56 (2007) (conclusory allegations are insufficient to satisfy the pleading standard).

Contrary to Plaintiffs' attempt to distinguish *Moscato v. TIE Technologies, Inc.*, No. 04 Civ. 2487 (GBD), 2005 WL 146806, at *6 (S.D.N.Y. Jan. 21, 2005), by claiming that the *Moscato* court "did not proceed to the analysis of any alleged breach" (Pl. Opp. at 24, n.19), the court clearly held that the plaintiff "failed to factually allege how he was owed a fiduciary duty by [the defendant] ***and*** in what way [the defendant] breached that duty." *Id.* (emphasis added). Like the plaintiff in *Moscato*, Plaintiffs have failed to allege facts establishing the existence of a

[8] Equally unavailing is Plaintiffs' reliance on *People v. Merkin*, No. 450879/09, 2010 WL 936208, at *5 (Sup. Ct. N.Y. County Feb. 8, 2010). In *Merkin*, the plaintiffs specifically alleged that an investment advisor of a fund made direct misrepresentations to the plaintiffs regarding their investments and the investment advisor's role in managing the funds. *Id.* at *2, 3-6. Unlike *Merkin*, the SCAC is devoid of any allegations that Pilgrim ever made any misrepresentation to Plaintiffs.

fiduciary duty ***or*** how Pilgrim breached that duty.[9]

C. Plaintiffs Lack Standing to Bring Their Claim Against Pilgrim Because That Claim Is Derivative

Plaintiffs seek to hold Pilgrim responsible for losses resulting from Madoff's fraud solely on the basis of FGBL's alleged mismanagement of the Fairfield Funds and Pilgrim's service as a director of FGBL. (SCAC ¶¶ 561-562.)[10] Yet, such claims are necessarily derivative under both Delaware law and the law of the British Virgin Islands ("BVI"), because Plaintiffs cannot show an injury that is independent from that suffered by the Fairfield Funds.

The recent case of *Stephenson*, another Madoff-related suit brought by an investor in Greenwich Sentry (one of the Fairfield Funds here), illustrates this point. In *Stephenson*, the court analyzed a breach of fiduciary duty claim (as well as other non-inducement claims) brought against CFSE and CCI for failing to discover Madoff's Ponzi scheme. *Id.* at *7-9. Judge Holwell held that, because the plaintiff could not prevail on such claims without showing an injury to the fund itself, his claims were derivative, not direct. *Id.* Plaintiffs' claim against Pilgrim fails for the same reason. Given that breach of fiduciary duty claims by hedge fund investors against a hedge fund's service providers are derivative in nature, certainly a claim by

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[9] Plaintiffs' reliance on *Automatic Catering, Inc. v. First Multifund for Daily Income, Inc.*, No. 80 Civ. 4117, 1981 WL 1664 (S.D.N.Y. Aug. 3, 1981), is misconceived. There, the court concluded that the existence of issues of fact regarding the plaintiffs' fraud-based breach of fiduciary duty claim, which was predicated on misrepresentations allegedly made by the defendant director (and others), prevented an award of summary judgment in the defendants' favor. *Id.* at *10. In contrast to *Automatic Catering*, Plaintiffs here do not allege that Pilgrim made any misrepresentation to Plaintiffs or had any contact with them whatsoever.

[10] Plaintiffs' allegations against Pilgrim are set forth in only two paragraphs of the 200-plus page SCAC, where Plaintiffs merely allege, in the most conclusory fashion imaginable, that Pilgrim breached his fiduciary duty "by failing to supervise the Funds' managers and investments that were entrusted to Madoff and in failing to pursue red flags that should have alerted [him] to the presence of unlawful activity." (SCAC ¶¶ 561-562.)

hedge fund investors against an individual who served as an outside director of a service provider of the hedge fund, even if legally cognizable, are likewise derivative.[11]

BVI law, which applies here because the BVI is the place of incorporation of Fairfield Sentry and Fairfield Sigma, compels the same result. *See Stephenson*, 2010 WL 1244007, at *7 (citing *DeBussy LLC v. Deutsche Bank AG*, No. 05 Civ. 5550, 2006 WL 800956, at *3 (S.D.N.Y. Mar. 29, 2006) ("When deciding issues of 'shareholder standing,' that is, whether claims should be brought directly or derivatively, courts must look to the law of the fund's state of incorporation.")). Under BVI law, claims for injuries to a shareholder derived from injuries to the corporation belong to the corporation. (*See* FGG Opening Memorandum at 12-17; Affidavit of Gerard Farara, ¶ 24.) Plaintiffs' Opposition (FGG) and the Affidavit of Robert Miles, Q.C., do not refute this rule, or the BVI rule of law that mismanagement claims are derivative. In fact, Mr. Miles' Affidavit, which merely suggests that fraudulent inducement claims are not derivative (Miles Aff. ¶ 25), is irrelevant because Pilgrim is not alleged to have made any fraudulent representations to Plaintiffs or to have had any contact with them at all.[12]

For these reasons, and those raised in the FGG Defendants' Reply Memorandum addressing the issue of standing, which is incorporated by reference, Plaintiffs' breach of

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[11] The *Stephenson* court applied *Tooley v. Donaldson, Lufkin, & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004), noting that a claim for mismanagement "represents a direct wrong to the corporation that is indirectly experienced by all shareholders. Any devaluation of stock is shared collectively by all the shareholders, rather than independently by the plaintiff or any individual shareholder. Thus, the wrong alleged is entirely derivative in nature." *Stephenson*, 2010 WL 1244007, at *9.

[12] For the same reason, Plaintiffs' reliance on *Pension Committee of the University of Montreal Pension Plan v. Banc of America Securities, LLC*, 592 F. Supp. 2d 608 (S.D.N.Y. 2009), *Pension Committee of the University of Montreal Pension Plan v. Banc of America Securities, LLC*, 446 F. Supp. 2d 163 (S.D.N.Y. 2006), and *Cromer Finance Ltd. v. Berger*, 137 F. Supp. 2d 452 (S.D.N.Y. 2001), is unavailing. These decisions addressed alleged misrepresentations by the defendants directly to the plaintiffs, which is not the case here. Moreover, standing was not even an issue in *Cromer*.

fiduciary claim against Pilgrim should be dismissed because it is derivative and Plaintiffs lack standing to assert it.

D. Plaintiffs' Breach of Fiduciary Duty Claim Is Time-Barred

There can be no serious dispute that the breach of fiduciary duty claim against Pilgrim is barred by C.P.L.R. Section 214(4)'s three-year limitations period. The claim against him is based on allegedly negligent conduct while he served as a director of FGBL. (SCAC, ¶¶ 560-565.) Pilgrim ceased serving as a director in 2005. (*Id*. ¶ 164.) He was first named as a defendant in this action in 2009 – more than three years after his service as a director ended. He is not alleged to have fraudulently concealed his purported breach between 2005 and 2009.[13] Because the statute of limitations for negligence-based breach of fiduciary duty claims seeking monetary damages is three years, and because such claims accrue upon the date of the alleged breach, Plaintiffs' breach of fiduciary claim against Pilgrim is time-barred. *Ciccone v. Hersh*, 530 F. Supp. 2d 574, 579 (S.D.N.Y. 2008), *aff'd*, 320 F. App'x 48 (2d Cir. 2009); *see also* C.P.L.R. § 203(a).

[13] Plaintiffs' reliance on *Golden Pacific Bancorp v. Federal Deposit Insurance Corp.*, 273 F.3d 509, 518-19 (2d Cir. 2001), is misplaced. That case analyzed C.P.L.R. 213(2) and (7), not 214(4), which is not tolled by the open repudiation doctrine. *Kaszrier v. Kaszirer*, 286 A.D.2d 598, 598-99 (1st Dep't 2004). In any event, *Golden Pacific* recognizes that "the limitations period for claims arising out of a fiduciary relationship does not commence 'until the fiduciary has openly repudiated his or her obligation ***or the relationship has been otherwise terminated***.'" 273 F.3d at 518-19 (emphasis added). The termination of Pilgrim's tenure as a FGBL director in 2005 thus commenced the limitations period under Plaintiffs' own analysis. Further, Plaintiffs' argument that the SCAC relates back to the filing date of the *Inter-American* Complaint is a red herring. Plaintiffs expressly allege that Pilgrim's tenure as a director of FGBL ended in 2005, more than three years before the *Inter-American* Complaint was filed. (SCAC ¶ 164.) Thus, neither the relation back doctrine nor the January 12, 2009 filing date of the *Inter-American* Complaint avoids the outcome that the claim against Pilgrim is time-barred.

II. The SCAC Provides No Basis for Imposing *Respondeat Superior* or Agency Liability on CFSB

Plaintiffs have not alleged (nor can they) that CFSB served as an administrator, custodian, bank, or in any other capacity in relation to the Fairfield Funds, or that it had any contact with any Plaintiff. Instead, all their claims against CFSB are based either on *respondeat superior* or agency theories, neither of which find the slightest support in the SCAC.

In its Opening Memorandum, CFSB cited established precedent demonstrating that a *respondeat superior* claim predicated on an employee's service as a director of a separate company is outside the scope of the employee's employment in the absence of concrete allegations of agency and control. *See* Pilgrim Opening Memorandum at 12-13; *In re Global Crossing, Ltd. Sec. Litig.*, No. 02 Civ. 910 (GEL), 2005 WL 2990646, at *5-6 (S.D.N.Y. Nov. 7, 2005); *In re Global Crossing, Ltd. Sec. Litig.*, No. 02 Civ. 910 (GEL), 2005 WL 1881514, at *3-4, 9-11 (S.D.N.Y. Aug. 5, 2005). Plaintiffs neither rebut that rule of law, distinguish the *Global Crossing* holdings,[14] nor cite to any authority holding an employer liable under *respondeat superior* simply because one of its employees served on the board of a separate company and allegedly commited a tort. Nor do Plaintiffs offer any factual allegations establishing that CFSB controlled Pilgrim or Francoeur's activities as directors of FGBL.[15]

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[14] Plaintiffs provide no reason why *Global Crossing* does not control. They do not explain why an employer that appoints directors to another company under its right to do so as a minority shareholder should be treated differently for *respondeat superior* purposes than an employer that appoints a director to the board of a customer of the employer.

[15] Plaintiffs' reliance on *Riviello v. Waldron*, 47 N.Y.2d 297 (N.Y. 1979), and *Lundberg v. State*, 25 N.Y.2d 467 (N.Y. 1969), is misplaced. Neither case addresses a company's liability under *respondeat superior* for allowing an employee to serve on the board of another company. Rather, the cases generically focus on the "test" for whether employee actions while working directly for their employers were within the scope of their employment. *See Riviello*, 47 N.Y.2d at 303-05 (employer was liable when its cook/bartender negligently handled a knife causing a patron to lose an eye); *Lundberg*, 25 N.Y.2d at 470-72 (State of New York could not be held

Plaintiffs' agency-based claims are equally deficient. Plaintiffs recognize that in order to plead an actual agency theory, they must allege facts demonstrating (i) a manifestation by the principal to have the agent act on the principal's behalf, (ii) the agent's acceptance, and (iii) control by the principal of the agent's acts. (Pl. Opp. at 50.) Yet Plaintiffs have alleged no facts to support a claim that any "Citco company" agreed to serve as CFSB's agent and that CFSB controlled the actions of any "Citco Company." Rather, Plaintiffs allege only that Pilgrim, Francoeur, and CFSB acted as the agents of CGL and the other "Citco Defendants," and that each "Citco company" acted as the agent of CGL and each other. (SCAC ¶¶ 156, 323, 564.) These conclusory allegations fall far short of establishing the requisite manifestation of agreement and control. *Spagnola v. Chubb Corp.*, 264 F.R.D. 76, 89-90 (S.D.N.Y. 2010); *Maung Ng We v. Merrill Lynch & Co., Inc.*, No. 99 Civ. 9687 (CSH), 2000 WL 1159835, at *5-9 (S.D.N.Y. Aug. 15, 2000). For these reasons, as well as those set forth in CGL's Reply Memorandum, Plaintiffs' agency-based claims should be dismissed.[16]

CONCLUSION

For the foregoing reasons, Pilgrim and CFSB respectfully request that the Court dismiss all claims asserted against them in the SCAC with prejudice.

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liable for employee's negligence while driving his car because the employee was not driving in furtherance of his work).

[16] Alternatively, all of the state law claims for which Plaintiffs allege CFSB is liable on an agency basis should be dismissed as preempted by SLUSA and the Martin Act, as well as the other grounds set forth in the CGL, CFSE/CCI, and CBN/CGC Reply Memoranda. For any arguments or discussion not presented here, CFSB relies on its Opening Memorandum and the applicable Reply Memoranda of Law of the other Defendants. All grounds for dismissal are expressly preserved.

Dated: May 21, 2010

Respectfully submitted,

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