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 OF LAW IN SUPPORT OF DEFENDANTS CITCO BANK NEDERLAND N.V. DUBLIN BRANCH AND CITCO GLOBAL CUSTODY N.V.'S MOTION TO DISMISS THE SECOND CONSOLIDATED AMENDED COMPLAINT

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Case(s) **Page(s)**

Statute and Rule(s) **Page(s)**

INTRODUCTION

In their Opposition,[1] Plaintiffs seek to evade the consequences of claiming to be third-party beneficiaries of the Custody Agreements between CBN and CGC and Fairfield Sentry and Fairfield Sigma (the "Fairfield Funds" or the "Funds"). Yet, by asserting the Funds' right to enforce the Custody Agreements, Plaintiffs are bound by the material terms of these agreements, including the forum selection clauses that require that all claims against CBN and CGC be adjudicated in The Netherlands. As a result, the claims should be dismissed in favor of The Netherlands forum.

If Plaintiffs' claims are litigated in this forum, they should be dismissed with prejudice. Plaintiffs lack standing to bring their claims because they are derivative of the claims of the Funds. In addition, Plaintiffs' claims are preempted under the Martin Act. Finally, CBN and CGC were not fiduciaries to Plaintiffs and owed them no duty in performing the services for the Funds set forth in the Custody Agreements.

ARGUMENT

I. PLAINTIFFS' CLAIMS AGAINST CBN AND CGC MAY ONLY BE LITIGATED IN THE NETHERLANDS

Plaintiffs raise several arguments in an effort to avoid the mandatory forum selection clauses in the very Custody Agreements which Plaintiffs themselves seek to enforce. For the reasons that follow, each of their arguments fails.

Plaintiffs argue that the mandatory forum selection clauses are limited to claims "brought by the Funds," and are therefore inapplicable to Plaintiffs' claims. (Pl. Opp. at 62.) This

[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 Citco Bank Nederland N.V. Dublin Branch and Citco Global Custody N.V.'s Motion to Dismiss the Second Consolidated Amended Complaint (D.E. 341). "Plaintiffs' Opp. (FGG)" refers to Plaintiffs' Consolidated Opposition to the Fairfield Greenwich Defendants' Motions to Dismiss (D.E. 418).

argument misses the essential point that as purported third-party beneficiaries, all of Plaintiffs' claims derive from the Defendants' contractual duties to the Fairfield Funds under the Custody Agreements. (*See* SCAC ¶¶ 474, 480.) Because any claims by the Fairfield Funds against CBN or CGC that "arise out of or are related" to the Custody Agreements must be brought in The Netherlands, any claims by Plaintiffs seeking enforcement of the duties Defendants owe to the Fairfield Funds under those same agreements must also be brought in that jurisdiction. *See Burrows Paper Corp. v. Moore & Assocs*., No. 6:07-CV-62, 2007 WL 2089682, at *3 (N.D.N.Y. July 20, 2007) ("[I]t would defy logic to allow plaintiff, as a third-party beneficiary, to seek the enforcement of some of the terms of the [agreement], e.g., those related to defendants' obligation[s] . . . while denying its obligations under others, e.g., the forum-selection clause.").[2]

Alternatively, Plaintiffs are also bound by the forum selection clauses because their claims are completely derivative of, and predicated upon, the Fairfield Funds' rights under the Custody Agreements. *See Weingrad v. Telepathy, Inc*., No. 05 Civ. 2024 (MBM), 2005 WL 2990645, at *5 (S.D.N.Y. Nov. 7, 2005) (dismissing complaint for improper forum, reasoning that "[a] non-party is 'closely related' to a dispute if its interests are 'completely derivative' of and 'directly related to, if not predicated upon' the signatory party's interests or conduct."). In this case, the standard is met because each Plaintiff is asserting a "general breach of the contracts

[2] *Maritime Insurance Co. Ltd. v. M/V "Sea Harmony"*, No. 97 CIV. 3818 (SHS), 1998 WL 214777 (S.D.N.Y. May 1, 1998), does not support Plaintiffs' argument. (Pl. Opp. at 63.) In *Maritime*, the court declined to enforce a forum selection clause in a bill of lading against a defendant, finding that it was not a third-party beneficiary to all the terms of the bill of lading, but only to a single clause that did not include a forum selection provision. *Id.* at *2. *Novak v. Tucows, Inc.*, No. 06-CV-1909 (JFB) (ARL), 2007 WL 922306 (E.D.N.Y. Mar. 26, 2007), *aff'd*, 330 F. App'x 204 (2d Cir. 2009), actually undercuts Plaintiffs' position. (Pl. Opp. at 64 n.50.) The court's discussion and analysis of the applicability of forum selection clauses noted specifically that third-party beneficiaries, such as Plaintiffs purport to be in this case, are "'closely related' to the dispute at issue and 'foreseeably' bound by the forum-selection clause." *Id.* at *13 n.11 (collecting cases).

that is applicable to the partnership at large, and as such he could not demonstrate his own injury without demonstrating that the partnership was injured." *See Stephenson v. Citco Group Limited*, No. 09 CV 00716 (RJH), 2010 WL 1244007, at *9 (S.D.N.Y. April 1, 2010) (dismissing with prejudice Greenwich Sentry investor's claim for third-party beneficiary breach of contract against Citco-related Defendants as derivative of the Fund's claim); *see also infra* pp. 5-7; CBN and CGC Opening Memorandum at 19.[3]

Ignoring the applicable legal standard, Plaintiffs seek to avoid the forum selection clauses by claiming that they were not "reasonably communicated" to them. However, the applicable standard, as affirmed by the Second Circuit in *Aguas Lenders Recovery Group LLC v. Suez, S.A.*, 585 F.3d 696, 701-02 (2d Cir. 2009), is that the party be "closely related" to the dispute, such that it is "foreseeable" that it would be bound. Because Plaintiffs claim to be third-party beneficiaries, and because Plaintiffs' claims are derivative of the rights of the Fairfield Funds, Plaintiffs, by definition, satisfy the "closely related" and "foreseeability" standard. *See BNY AIS Nominees Ltd. v. Quan*, 609 F. Supp. 2d 269, 275-76 (D. Conn. 2009) (citing *Roby v. Corp. of Lloyd's*, 996 F.2d 1353 (2d Cir. 1993)); *Weingrad*, 2005 WL 2990645, at *5.[4] This makes perfect sense because it is clearly foreseeable to any plaintiff seeking enforcement of some of the terms of a contract that it would be bound by the obligations set forth in other terms.

Plaintiffs also erroneously contend that the broad language of the forum selection clauses should be construed narrowly so as to exclude all of Plaintiffs' tort claims. (Pl. Opp. at 62-63.)

[3] For this reason, even if Plaintiffs are not third-party beneficiaries of the Custody Agreements, they are nevertheless bound by the forum selection clause of those agreements because their claims are derivative.

[4] *Shea Development Corp. v. Watson*, No. 07 Civ. 11201 (DLC), 2008 WL 762087 (S.D.N.Y. Mar. 24, 2008), on which Plaintiffs rely (Pl. Opp. at 63), is inapposite. There, the court found that a defendant was not bound by a forum clause in an acquisition agreement because she did not claim to be a third-party beneficiary or otherwise purport to assert any rights derived from the agreement. *Id.* at *2-3.

However, because the forum selection clauses at issue encompass all proceedings or claims "arising out of or ***related to*** [the Custody Agreements]" (emphasis added), they must be read expansively. It is for this very reason that Plaintiffs' reliance on *Phillips v. Audio Active Ltd.*, 494 F.3d 378 (2d Cir. 2007), is misplaced. In *Phillips*, the Second Circuit analyzed a forum selection provision that required "any legal proceedings that ***may arise out of***" the contract to be brought in England. *Id.* at 386-87 (emphasis added). Construing the term "arise out of" narrowly, the court held that the forum selection clause only covered contract claims. *Id*. at 387-91. Significantly, however, the court observed that forum selection clauses containing the broader "related to" language (such as the forum selection clauses at issue here) would encompass both contract ***and*** non-contract claims. *Id.* at 389; *see also Fin. One Pub. Co. Ltd. v. Lehman Bros. Special Fin., Inc.*, 414 F.3d 325, 335 (2d Cir. 2005) (forum-selection clause covering any action "relating to this Agreement" governed contractual and extra-contractual claims). Here, Plaintiffs' tort claims "relate to" the Custody Agreements because they are expressly based on allegations that CBN and CGC did not adequately perform their duties under the Custody Agreements. (*See, e.g.*, SCAC ¶ 496 as to breach of fiduciary duty; ¶¶ 502, 506 as to gross negligence and negligence; and ¶¶ 512, 518 as to the aiding and abetting claims.) Accordingly, all of Plaintiffs' claims are within the broad scope of the forum selection clauses.[5]

Plaintiffs' attempt to parse the language of the forum selection clauses (Pl. Opp. at 61-62), is irrelevant in light of the above discussion. Even Plaintiffs concede that the forum clauses are mandatory as to the Funds. (Pl. Opp. at 62.) As noted above, because Plaintiffs are asserting

[5] Courts in this circuit regularly apply forum selection clauses to both contract and tort claims that relate to the parties' contractual relationship. *See, e.g., Bense v. Interstate Battery Sys. of Am., Inc.*, 683 F.2d 718, 720-22 (2d Cir. 1982); *Korean Press Agency, Inc. v. Yonhap News Agency*, 421 F. Supp. 2d 775, 781 (S.D.N.Y. 2006).

the contractual rights of the Funds by claiming to be third-party beneficiaries of the Custody Agreements, and because their claims are derivative of the claims of the Funds, the forum clauses are equally mandatory as to them. *See Falik v. Smith*, 884 F. Supp. 862, 868 n.3 (S.D.N.Y. 1995) ("It stands to reason, however, that [plaintiff] can not invoke the benefits of the agreement, that is, indemnity, while abdicating its jurisdictional provisions.") (citing *Benson v. Brower's Moving & Storage, Inc.*, 907 F.2d 310, 313 (2d Cir. 1990) (third-party beneficiaries "step into the shoes of the promisee")).

II. EVEN IF ADJUDICATED IN NEW YORK, PLAINTIFFS' CLAIMS AGAINST CBN AND CGC FAIL

A. Plaintiffs Lack Standing Because Their Claims Against CBN and CGC Are Derivative

Plaintiffs' state law claims against CBN and CGC (Counts 20-24, 32, 33), which are premised on the assertion that "Citco" failed to "monitor" Madoff (Pl. Opp. at 2; SCAC ¶¶ 159, 160, 485, 496), are derivative of the Fairfield Funds' claims. Because Plaintiffs lack standing to assert those claims, they should be dismissed. The *Stephenson* case is directly on point. In that decision, Judge Holwell, applying the test set forth in *Tooley v. Donaldson, Lufkin, & Jenrette, Inc.*, 845 A.2d 1031 (Del. 2004), dismissed all of the non-inducement claims of a Greenwich Sentry investor against CGL, CSFE, and CCI. *Stephenson*, 2010 WL 1244007, at *7-9. Judge Holwell held that, because the plaintiff could not prevail on such claims without showing injury to the fund itself, the claims were derivative and he lacked standing to assert them. *Id.* at *9.

The determination of whether an injury is derivative or direct in nature is materially the same under Delaware law, as applied by Judge Holwell in *Stephenson*, as it is under the law of the British Virgin Islands ("BVI"), which applies here because the BVI is the place of incorporation of Fairfield Sentry and Fairfield Sigma. *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 Defendants' Opening Memorandum at 12-17, and the accompanying Affidavit of Gerard Farara setting forth BVI law at ¶ 24.) Plaintiffs' Opposition and the principles of BVI law set forth in the Affidavit of Robert Miles, Q.C., relating to fraudulent inducement or misrepresentation claims, are irrelevant to the derivative nature of their non-inducement based claims against CBN and CGC. That is because neither CBN nor CGC are alleged to have made ***any*** representations to Plaintiffs that induced them to do anything.[6]

Because the claims against CBN and CGC for breach of (and aiding and abetting) fiduciary duty, breach of (third-party beneficiary) contract, negligence, and gross negligence do not allege an injury independent of the injury to the Fairfield Funds, Plaintiffs lack standing to assert them.[7]

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[6] To the extent Plaintiffs attempt to rely on an agency theory to assert inducement claims, such as negligent misrepresentation, against CBN or CGC, such efforts should fail because the SCAC does not allege any facts to support a finding that CGL, CFSE, CCI or CFSB acted as CBN's or CGC's agent. Similarly, Plaintiffs cannot rely on agency principles to support their claim for aiding and abetting fraud. *See* CGL's Reply Memorandum at 5-8.

[7] Plaintiffs' citation to *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), *Cromer Finance Ltd. v. Berger*, 137 F. Supp. 2d 452 (S.D.N.Y. 2001), and *Pension Committee*, 592 F. Supp. 2d 608 (S.D.N.Y. 2009), for the proposition that "numerous cases . . . have recognized that fund investors hold direct claims against fund service providers" (Pl. Opp. at 56), is misconceived. Standing was not addressed in *Pension Committee*, 592 F. Supp. 2d 608 or *Cromer* and, in *Pension Committee*, 446 F. Supp. 2d 163, each plaintiff alleged inducement–based claims against a fund administrator for disseminating allegedly misleading NAV statements.

B. The Martin Act Preempts All of Plaintiffs' Non-Fraud Common Law Tort Claims

It is a settled issue in the Second Circuit that the Martin Act preempts private non-fraud common law claims in the securities context, including Plaintiffs' claims here. *Castellano v. Young & Rubicam, Inc.*, 257 F.3d 171, 190 (2d Cir. 2001). Indeed, every court addressing this issue in the context of the "feeder funds" that invested in Madoff's Ponzi scheme has dismissed all non-fraud common law claims as preempted by the Martin Act. *See Stephenson*, 2010 WL 1244007, at *15; *Meridian Horizon Fund, LP v. Tremont Group Holdings, Inc.*, No. 09 Civ. 3708 (TPG), 2010 WL 1257567, at *9 (S.D.N.Y. Mar. 31, 2010); *In re Tremont Sec. Law, State Law and Ins. Litig.*, 08 Civ. 11117 (TPG), 2010 WL 1257580, at *8 (S.D.N.Y. Mar. 30, 2010); *Barron v. Igolnikov*, No. 09 Civ. 4471 (TPG), 2010 WL 882890, at *6 (S.D.N.Y. Mar. 10, 2010). In so doing, these courts have noted that the cases on which Plaintiffs rely on pages 99-101 of their Opposition (FGG) – *Caboara v. Babylon Cove Development, LLC, Scalp & Blade, Inc. v. Advest, Inc.*, and *Cromer Finance Ltd. v. Berger* – "have been rejected repeatedly by courts in this district," or in the case of *Kerusa*, actually "support [ ] the traditional application of preemption to claims that are covered by § 352-c of the Martin Act."[8] *See Meridian Horizon Fund, LP*, 2010 WL 1257567, at *8; *Stephenson*, 2010 WL 1244007, at *12-13.

In these recent Madoff-related decisions, the courts have all found a sufficient nexus with New York to support Martin Act preemption, even as to claims by investors against non-U.S. service providers of offshore hedge funds. *See, e.g., Meridian Horizon Fund, LP*, 2010 WL

[8] *Caboara v. Babylon Cove Dev., LLC*, 862 N.Y.S.2d 535, 538-39 (2d Dep't 2008); *Scalp & Blade, Inc. v. Advest, Inc.*, 722 N.Y.S.2d 639, 640 (4th Dep't 2001); *Cromer Fin. Ltd. v. Berger*, No. 00 Civ. 2498, 2001 WL 1112548, at *4-5 (S.D.N.Y. Sept. 19, 2001); *Kramer v. W10Z/515 Real Estate Ltd. Partnership*, 844 N.Y.S.2d 18, 19-21 (1st Dep't. 2007), *rev'd on other grounds sub nom. Kerusa Co. LLC v. W10Z/515 Real Estate Ltd. Partnership*, 906 N.E.2d 1049 (N.Y. 2009). By contrast, in the case at bar, CBN and CGC never disseminated anything to Plaintiffs.

1257567, at *9 (dismissing foreign investors' claims against Cayman-based service providers of fund that invested with Madoff); *Barron*, 2010 WL 882890, at *6 (dismissing claims against investment manager and its Swiss parent as preempted because allegations centered on failure to perform due diligence on Madoff's operations).

Plaintiffs attempt to resist Martin Act preemption by arguing that Fairfield Sentry and Fairfield Sigma were sold to foreign investors and that the Citco Defendants' operations were run from outside the United States. (Pl. Opp. at 40.) Yet, as Judge Holwell noted in dismissing the claims of a Greenwich Sentry investor against various Citco entities that are defendants here: "a transaction is 'within or from' New York for purposes of the Martin Act if a plaintiff alleges that a 'substantial portion' of the events giving rise to a claim occurred in New York." *Stephenson*, 2010 WL 1244007, at *14 (internal citations omitted); *see also CRT v. Merkin*, No. 601052/09, slip op. at 10 (N.Y. Sup. May 5, 2010) (Martin Act preempted claims by foreign plaintiffs against the general partner and investment manager of Madoff-related funds).

The same types of contacts deemed dispositive in *Stephenson*, *Meridian Horizon* and *Barron* are all present here. With respect to ***all*** the Fairfield Funds, Defendant FGG (the name under which all of the corporate Fairfield Defendants were alleged to have operated), "maintain[ed] its principal office in New York." (SCAC ¶ 117; Fairfield Sentry 2003 PPM at 7.) Similarly, virtually all the individuals who are alleged to have overseen the business of the domestic ***and*** offshore Funds, or who are alleged otherwise to have participated in "creat[ing] and/or disseminat[ing] materially false and misleading documents," resided and/or were based in New York. (SCAC ¶¶ 124-129, 133, 134, 144, 150, 151.) Even the Fairfield Defendants who are alleged to have overseen the Funds' overseas marketing efforts resided and/or were based in New York. (*Id.* at ¶¶ 136-138, 140.)

It is also significant that Madoff's Ponzi scheme, out of which "this suit arises," was centered in New York, where Madoff and BLMIS created their false securities transactions, and where the Fairfield Funds handed over billions of dollars of investors' money to Madoff and BLMIS. (*See* SCAC ¶¶ 1, 159-160; 166; 170-173; 175.) *See Stephenson*, 2010 WL 1244007, at *1, 2, 14-15; *Meridian Horizon Fund, LP*, 2010 WL 1257567, at *2, 8; *see also Barron*, 2010 WL 882890, at *6. In fact, Plaintiffs concede the nexus with New York in their Opposition, arguing that "a substantial part of the events and actions of the Defendants giving rise to Plaintiffs' claims occurred in New York" (Pl. Opp. (FGG) at 47); the "substantial wrongdoing at the core of the claims occurred in New York" (*Id.* at 103 n.86); and "the information which the Citco Defendants failed to verify, in breach of their fiduciary and other duties, issued from Madoff in New York." (Pl. Opp. at 21; SCAC ¶¶ 157-160.) Thus, Plaintiffs' claims for breach of fiduciary duty, gross negligence, negligence, and aiding and abetting breach of fiduciary duty are preempted by the Martin Act.

C. Plaintiffs' State Law Claims Are Otherwise Legally Deficient

Various state law claims asserted against CBN and CGC are deficient for additional reasons as well. Plaintiffs' breach of fiduciary duty claim fails because the SCAC does not allege any acts on the part of CBN or CGC that would establish a fiduciary relationship with Plaintiffs, nor have Plaintiffs cited a single case where a hedge fund custodian was found to owe a fiduciary duty to fund investors with whom, as here, it had no contact or communication and to whom it rendered no services.[9] In addition, because there are no factual allegations in the SCAC

[9] The cases cited by Plaintiffs for the proposition that "Courts impose fiduciary duties on custodians of assets in various other contexts" (Pl. Opp. at 18 n.11) are inapposite because, in each of those cases, the custodians (or other fiduciaries) were custodians of the ***plaintiffs'*** assets. In contrast, in this case, CBN and CGC were custodians of ***the Funds'*** assets. Moreover, in

that CBN or CGC had actual knowledge of any breach of fiduciary duty or fraud on the part of the FGG Defendants, Plaintiffs have failed to state a claim for aiding and abetting either breach of fiduciary duty or fraud.[10] *See Rosner v. Bank of China*, No. 06 CV 13562, 2008 WL 5416380, at *7 (S.D.N.Y. Dec. 18, 2008) (expressly rejecting the "willful blindness" standard urged by Plaintiffs here, the court noted that the willful blindness standard "concedes a lack of actual knowledge").

CONCLUSION

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

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those cases, the plaintiffs had contacts and communications with the defendant custodians. Here, Plaintiffs had no such contacts or communications with CBN or CGC.

[10] For any arguments or discussion not presented here, CBN and CGC rely on their 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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