UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

In re HERALD, PRIMEO and THEMA FUNDS SECURITIES LITIGATION

This Document Relates To:

09-cv-289 and 09-cv-2032 (GBD)

Master File No. 09 Civ. 289 (RMB) (HBP)

DECLARATION OF MARC A. WEINSTEIN IN SUPPORT OF THE ERNST & YOUNG DEFENDANTS' MOTION TO DISMISS THE COMPLAINTS AND IN OPPOSITION TO PLAINTIFFS' MOTION FOR LEAVE TO AMEND THE COMPLAINTS

Marc A. Weinstein, pursuant to 28 U.S.C. § 1746, declares under penalty of perjury as follows:

1. I am a member of the Bar of this Court and of the firm Hughes Hubbard & Reed LLP, attorneys for Defendant Ernst & Young Ltd. ("EY Cayman"). I submit this declaration in support of the motions of EY Cayman, Ernst & Young, S.A. ("EY Lux"), and Ernst & Young Global Limited ("EYG") (collectively the "EY Defendants") to dismiss the Complaints.[1]

2. **Claims Against the EY Defendants**: The Complaints allege the following roles by the EY Defendants: EY Cayman issued audit reports for the Herald SPC and Primeo Funds. EY Lux was engaged to audit Herald Lux's 2008 financial statements, but *never issued an audit report* because Madoff's fraud was exposed before year-end. EY Cayman and EY Lux are local member firms of EYG, but there is no allegation that EYG, which does not serve any audit clients, participated in any challenged audit.

3. The Herald Complaint ("HC") asserts the following claims against the EY Defendants: (i) Civil conspiracy; (ii) Gross negligence (EY Cayman and EYG only); (iii) Negligence (EY Cayman and EYG only); (iv) Aiding and abetting fraud; (v) Aiding and abetting breach of fiduciary duty; and (vi) Aiding and abetting conversion. The Primeo Complaint ("PC") asserts the following claims against EY Cayman and EYG: (i) Fraud; (ii) Negligent misrepresentation; (iii) Gross negligence; (iv) Negligence; and (v) Aiding and abetting breach of fiduciary duty. The claims against the EY Defendants are nearly identical to those repeatedly dismissed in this Court and around the country as against auditors of Madoff-related funds. *See,*

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[1] This Declaration addresses the insufficiency of Plaintiffs' allegations under New York law. Defendants maintain that Plaintiffs' claims are governed by foreign law. (Joint Mem. § III.A.) The accompanying foreign law declarations of Jacques Delvaux and Graham Ritchie (attached hereto as Exhibits A and B) demonstrate that Plaintiffs' allegations against the EY Defendants are equally insufficient under the laws of Luxembourg and the Cayman Islands, respectively.

e.g., *In re Tremont Secs. Law, State Law, and Ins. Litig.*, 703 F. Supp. 2d 362 (S.D.N.Y. 2010). Each of the instant claims fails for the reasons set forth in the Joint Memorandum and for the additional reasons set forth below.

4. **Gross negligence, Negligence and Negligent Misrepresentation Claims:** These claims fail because there is no privity or "near privity" between the Funds' shareholders and the Funds' auditors. (Joint Mem. § III.B.1.) Plaintiffs merely allege that EY Cayman issued certain audit reports on the Funds' year-end financial statements. Plaintiffs do not even attempt to allege a "near privity" relationship with EYG. (*See* Joint Mem. § II.H.) Absent more, courts routinely dismiss such negligence claims against auditors.

5. To be liable in negligence to a third party, an auditor must know that "a primary, if not the exclusive, *end and aim* of auditing [the client] was to provide [the third party] with the financial information it required," *Credit Alliance v. Arthur Anderson*, 65 N.Y.2d 536, 554 (1985) (emphasis in original), and "must have known when preparing the [audit reports] that the *particular plaintiffs* bringing the action would rely on its representations," *SIPC v. BDO Seidman, LLP*, 222 F.3d 63, 75 (2d Cir. 2000) (emphasis in original). While both Complaints include conclusory assertions that EY Cayman knew that its audit reports would be "issued" or "provid[ed]" to shareholders who would rely upon them, (HC ¶¶ 713, 721; PC ¶¶ 260, 268), this does not satisfy the strict *Credit Alliance* test. The Complaints do not allege that EY Cayman issued any report specifically to or even knew of the existence of any particular shareholder.

6. Nor does the Complaint allege the requisite conduct linking EY Cayman to Plaintiffs. *See Credit Alliance*, 65 N.Y.2d at 551. Courts require affirmative "direct contact … such as face-to-face conversation, the sharing of documents or other 'substantive communication' between the parties." *BDO Seidman*, 222 F.3d at 75-76 (citation omitted); *see*

Credit Alliance, 65 N.Y.2d at 554. No such conduct is alleged on the part of EY Cayman, and the mere issuance of reports addressed to shareholders is plainly insufficient.[2] Accordingly, all negligence-based claims against the EY Defendants should be dismissed.

7. **Common Law Fraud**: The Joint Memorandum addresses the strict pleading standards for fraud claims. (*See* Joint Mem. § III.B.2.) "The standard for pleading auditor fraud is demanding." *CRT Invs., Ltd. v. Merkin*, 2010 WL 4340433, at *12 (Sup. Ct. N.Y. Cty. May 5, 2010) (dismissing fraud claim against auditor in Madoff suit). Against an outside auditor, allegations must "approximate an actual intent to aid in the fraud being perpetrated by the audited company." *S. Cherry St., LLC v. Hennessee Grp. LLC*, 573 F.3d 98, 110 (2d Cir. 2009).

8. In conclusory fashion, the Complaints recite a litany of auditing standards that EY Cayman purportedly violated. (*See, e.g.*, PC ¶¶ 111-139.) It is well-settled that alleged violations of professional and accounting standards without more are insufficient as a matter of law. *See Rothman v. Gregor*, 220 F.3d 81, 98 (2d Cir. 2000). Equally insufficient are allegations that "strongly suggest[] that the defendants should have been more alert and more skeptical." *Shields v. Citytrust Bancorp, Inc*., 25 F.3d 1124, 1129 (2d Cir. 1994); *see W. Virginia Inv. Mgmt. Bd. v. Doral Fin. Corp.*, 2009 WL 2779119, at *2 (2d Cir. Sept. 3, 2009). Where, as here, "[t]he gist of the Complaint against [the auditor] is an alleged failure to investigate," that '"[does] not rise above the level of negligence, which is legally insufficient.'" *O'Brien v. Nat'l Prop. Analysts Partners*, 719 F. Supp. 222, 228 (S.D.N.Y. 1989) (citation omitted).

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[2] *See CRT Invs., Ltd. v. BDO Seidman, LLP*, 2011 WL 2225050, at *2 (1st Dep't June 9, 2011); *William Iselin & Co. v. Landau*, 71 N.Y.2d 420, 427 (1988) ("[T]he single act of sending the Report at an undetermined time for an unknown purpose would not satisfy the burden of coming forth with evidence evincing [the auditor's] understanding of [third party's] reliance.").

9. The Complaints also recite a familiar list of supposed "red flags" of the kind that, absent knowledge, Judges Griesa, Holwell, McMahon, Marrero, and Sand have found insufficient to sustain a fraud claim against an auditor of a Madoff-related fund.[3] The Complaints do not allege that EY Cayman was responsible for auditing Madoff; indeed, the pleadings acknowledge that another firm, Friehling & Horowitz, was responsible for auditing Madoff's business, BMIS. No court has permitted a claim for fraud where "the [auditor was not] engaged to audit Madoff[']s businesses or to issue an opinion on the financial statements of BMIS," because "[t]he notion that a firm hired to audit the financial statements of one client . . . must conduct audit procedures on a third party that is not an audit client (BMIS) on whose financial statements the audit firm expresses no opinion has no basis." *In re Tremont*, 703 F. Supp. 2d at 371; *see also In re J.P. Jeanneret Associates*, 2011 WL 335594, at *31 ("No Madoff-related case of which this Court is aware has sustained a [fraud] claim against a feeder fund's outside auditors."). The fraud claim against EY Cayman and EYG should likewise be dismissed.

10. **Aiding and Abetting Claims**: All the aiding and abetting claims asserted against the EY Defendants are deficient because they fail to establish either actual knowledge of, or substantial assistance in, the purported acts of fraud, breach of fiduciary duty or conversion. (*See* Joint. Mem. § III.B.4.) The Complaints fail to offer any non-conclusory allegations that any EY party had actual knowledge of the alleged wrongdoing. In fact, the Complaints state no facts regarding EY Lux's or EYG's knowledge at all, and those asserted against EY Cayman do not

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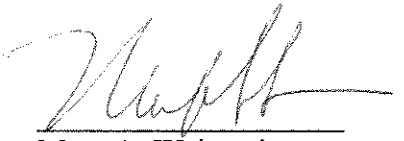
[3] *See Stephenson v. PricewaterhouseCoopers, LLP*, 2011 WL 781936, at *8 (S.D.N.Y. Mar. 6, 2011); *In re J.P. Jeanneret Assocs., Inc*., 2011 WL 335594, at *31 (S.D.N.Y. Jan 31, 2011); *Saltz v. First Frontier, LP*, 2010 WL 5298225 (S.D.N.Y. Dec. 23, 2010); *Anwar v. Fairfield Greenwich Ltd.*, 728 F. Supp. 2d 372 (S.D.N.Y. 2010); *Meridian Horizon Fund, LP v. Tremont Group Holdings, Inc*., 747 F. Supp. 2d 406 (S.D.N.Y. 2010); *In re Tremont,* 703 F. Supp. 2d 362; *In re Beacon Assocs. Litig.*, 745 F. Supp. 2d 386 (S.D.N.Y. 2010).

remotely approach actual knowledge. Nor do the Complaints allege that any EY Defendant provided substantial assistance in the alleged offenses. EYG and EY Lux issued no audit opinions, and the EY Cayman audit opinions issued to the funds were ordinary business functions which are insufficient.

11. **Statute of Limitations**: New York has three-year statute of limitations for claims of negligence and accounting malpractice. N.Y. C.P.L.R. §§ 214(4)-(6) (2009). This applies to all of Plaintiffs' state law claims notwithstanding their various labels because each claim seeks monetary relief based upon EY Cayman's alleged failure to adequately perform auditing services. *See, e.g., Levin v. PricewaterhouseCoopers, LLP*, 302 A.D.2d 287, 287 (1st Dep't 2003) (aiding and abetting claim dismissed under the three-year statute of limitations). The limitations period accrues when an auditor issues its report. *See Williamson v. PricewaterhouseCoopers LLP*, 9 N.Y.3d 1, 8 (2007). EY Cayman was named as a defendant in these actions on March 19, 2009. Thus, claims based on any reports that EY Cayman issued before March 19, 2006 fall outside the three-year limitations period and are time-barred.

12. **Forum Non Conveniens**: As noted in the Joint Memorandum, to the extent the Court dismisses the claims on grounds of *forum non conveniens*, EY Cayman and EYG consent to jurisdiction in the Luxembourg courts over the claims asserted herein. This consent is limited to the specific claims asserted in the Complaints by individual shareholders on their own behalf and on behalf of putative class members. EY Cayman and EYG do not consent to the jurisdiction of the Luxembourg courts for any claims brought by or on behalf of the Funds (whether asserted by a liquidator or individual shareholders on a derivative basis).

Executed on June 29, 2011



Marc A. Weinstein