

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

IN RE HERALD, PRIMEO AND THEMA
FUNDS SECURITIES LITIGATION

This documents relates to: All Actions

ECF CASE

Civil Action No. 09 Civ. 0289 (RMB)
(Consolidated with Nos. 09 Civ. 2032 and
09 Civ. 2558)

**ATTORNEY DECLARATION OF EVAN A. DAVIS
IN SUPPORT OF THE HSBC DEFENDANTS' MOTION TO DISMISS**

CLEARY GOTTlieb STEEN & HAMILTON LLP

Evan A. Davis
One Liberty Plaza
New York, New York 10006
(212) 225-2000

Counsel for Defendants HSBC Holdings plc, HSBC Securities Services (Luxembourg) S.A., Bank of Bermuda (Luxembourg) S.A., Bank of Bermuda (Cayman) Limited, The Bank of Bermuda Limited, HSBC Institutional Trust Services (Ireland) Ltd. ("HTIE"), and HSBC Securities Services (Ireland) Limited ("HSSI"), and Proposed Defendant HSBC Bank USA, N.A. (together, "HSBC" or the "HSBC Defendants")

I, Evan A. Davis, declare under penalty of perjury as follows:

1. I am a member of the bar of this Court and a partner at Cleary Gottlieb Steen & Hamilton LLP, counsel for the HSBC Defendants. I respectfully submit this declaration as a supplement to the Joint Brief in support of HSBC's motion to dismiss.

2. It is the HSBC Defendants' position that foreign law governs every claim asserted against them because such claims arise from administration and custody services that certain HSBC defendants acting in Ireland, Luxembourg and the Cayman Islands provided to the Funds. HSBC relies on the foreign law declarations attached to the Joint Brief and hereto.

3. When subscribing to the Funds, some, if not all, investors in Herald Lux and certain investors in Primeo agreed that "any dispute concerning [their] investment in the [Fund] will be settled in Luxembourg according to Luxembourg law." *See* Ex. 6, at 8; Ex. 7, at 9; Ex. 9, at 9. In addition, when subscribing to Herald SPC, some, if not all, investors agreed that Cayman law would govern their subscription form and also agreed to submit to the non-exclusive jurisdiction of the Cayman Islands. *See* Ex. 8, at 8.

4. In the event New York law is deemed to apply, this declaration sets forth the following particularized reasons why the Complaints' allegations against HSBC fail to state a claim under New York law, in addition to the reasons stated in the Joint Brief:

5. Plaintiffs' negligence-based claims – negligence, professional negligence, gross negligence, and negligent misrepresentation – fail because the Complaints merely state conclusory allegations, including that Plaintiffs had a "special relationship" with HSBC giving rise to a duty of care. PC Counts 13, 14, 16, 17, 24, 26, ¶¶ 297, 304, 321, 327; TC Counts 5, 7, 9, ¶¶ 464, 470, 476, 482; HC Counts 14, 15, ¶¶ 751, 758. The sole alleged basis for this "special relationship" is certain HSBC defendants' obligations to provide custody and administration

services *to the Funds* pursuant to written agreements *with the Funds*. PC ¶¶ 8, 147, 152, 304-05, 327-28; TC ¶¶ 102, 158, 162, 464, 470, 476, 482; HC ¶¶ 759-60, 762. The duties owed under these agreements flowed solely to the Funds and form no basis for a duty of care to the Funds' investors. *See* Joint Br. at 32-33. Accordingly, investors cannot assert direct claims. *In re Optimal U.S. Litig.*, ___ F. Supp. 2d ___, 2011 WL 1676067 at *13-14 (S.D.N.Y. May 2, 2011).

6. The absence of any sufficiently-pleaded special relationship also precludes Plaintiffs' claims for breach of fiduciary duty. PC Counts 12, 15, ¶¶ 287-95, 311-19; TC Count 13, ¶¶ 504-10; HC Count 13, ¶¶ 736-46. The day-to-day administration and custody functions performed by certain HSBC defendants for the benefit of the Funds and cited by Plaintiffs, *see* PC ¶¶ 287-289, 311-313; TC ¶¶ 504, 507; HC ¶¶ 736-40, establish nothing more than ordinary commercial relationships with the Funds, which are insufficient bases for fiduciary duties. *See* Joint Br. at 34. Absent non-conclusory supporting factual allegations of a special relationship, Plaintiffs' cursory allegations of reposing trust and confidence in HSBC service providers, *see* HC ¶¶ 741-42; PC ¶¶ 290-92, 314-16; TC ¶¶ 505-06, or about HSBC defendants' superior position, *see* HC ¶¶ 736, 741, 743-44; PC ¶¶ 287, 292-93, 312, 314, 317; TC ¶¶ 504, 506, fail to establish a fiduciary duty as a matter of law. *See Abercrombie v. Andrew College*, 438 F.Supp.2d 243, 274-75 (S.D.N.Y. 2006); *Suthers v. Amgen, Inc.*, 372 F.Supp.2d 416, 426-27 (S.D.N.Y. 2005). Plaintiffs also identify no statements or course of conduct by any HSBC defendant directed toward the Funds' investors that show the required assumption of responsibility on HSBC's part to act primarily on their behalf or for their benefit. *See* Joint Br. at 34.

7. The quasi-contractual claims – unjust enrichment (HC Count 16, ¶¶ 768-71; PC Count 18, ¶¶ 333-36; TC Count 19, ¶¶ 540-43) and constructive trust (TC Count 18, ¶¶ 535-38) –

fail because the Plaintiffs’ conclusory allegations of a “special relationship” between Plaintiffs and HSBC, discussed above, do not have a sufficient factual basis to establish any relationship; nor does the Thema Plaintiffs’ conclusory allegation that HSBC “had a fiduciary and/or confidential relationship” with Plaintiffs due to its contractual obligations, TC ¶ 535, establish the existence of any relationship, much less a fiduciary or confidential one. Joint Br. at 34, 37-38. Additionally, Plaintiffs’ quasi-contractual claims fail because the service fees earned by HSBC were paid by the Funds, not by investors, HC ¶ 528; PC ¶¶ 149, 333; TC ¶¶ 303; Joint Br. at 37, pursuant to valid administration and custodian contracts, the existence of which precludes quasi-contractual remedies, even for third parties. Joint Br. at 37-38.

8. The Primeo Plaintiffs’ claims for fraud fail because the Primeo Complaint inadequately states scienter with respect to the Administrator’s allegedly incorrect NAV calculations, *see* PC ¶¶ 147-50, 388, and with respect to the Custodians’ alleged lack of reasonable supervision of the correspondent, *see* PC ¶¶ 151-55, 396-98. PC Counts 23, 25.¹

9. The Thema and Herald Plaintiffs’ claims for aiding and abetting breach of fiduciary duty, and the Herald Plaintiffs’ claims for aiding and abetting fraud and aiding and abetting conversion, all fail for insufficient allegations under *Twombly* of actual knowledge, a predicate element of each of these causes of action. TC Count 15, ¶ 519; HC Counts 3, 18, 19, ¶¶ 657, 779, 790, 792, 797, 800, 802. *See* Joint Br. at 35-36. Compliance with that plausibility

¹ Further, the Primeo Plaintiffs’ attempt to attribute alleged misstatements about promised due diligence in the Primeo Offering Memorandum (“Primeo OM”) to the HSBC custodian fails because the Primeo OM states that the custodian is “not responsible” for statements contained therein. Ex. 11, at 19; *Pacific Inv. Mgmt. Co. v. Mayer Brown LLP*, 603 F.3d 144, 158 (2d Cir. 2010) (adopting the attribution standard for Rule 10(b) securities fraud claims). Moreover, the Primeo Plaintiffs themselves concede that HSBC conducted due diligence by twice engaging KPMG, *see* PC ¶¶ 161, 164, and therefore do not plausibly plead that the HSBC custodians had no intention of keeping such promise. *Abelman v. Shoratlantic Development Co.*, 545 N.Y.S.2d 333, 334 (N.Y. App. Div. 1989).

standard would require allegations of specific non-conclusory facts permitting the reasonable inference that the HSBC Defendants actually knew that Madoff was engaging in sham purchases. Nothing close to that appears in any of the Complaints. Moreover, Plaintiffs acknowledge that HSBC twice engaged KPMG to review BLMIS for fraud and related operational risk, *see* PC ¶¶ 161, 164; HC ¶¶ 502, 507; TC ¶¶ 179, 183, yet make no allegation that sham transactions or any other types of fraud was discovered. (Indeed, KPMG tested for sham transactions and found none.) The Thema Complaint refers to HSBC's participation in structured financial products, *see* TC ¶188, transactions through which HSBC invested in certain funds that invested in Madoff, yet makes no allegation that HSBC bailed out of these investments because of even a suspicion of fraud. (Indeed, HSBC lost nearly \$1 billion of its own money as a result of its investments in these funds.) In sum, Plaintiffs' aiding and abetting claims that depend on alleging actual knowledge of sham transactions utterly fail to meet *Twombly*'s requirements and, if persisted in, will raise serious Rule 11 concerns.

10. Additionally, Plaintiffs' conclusory allegations also do not establish with the particularity required by Rule 9(b) that HSBC had any actual knowledge of or even recklessly disregarded Madoff's fraud. There is no meaningful particularization of any of the HSBC Defendants' actual knowledge of the supposed red flags, and, without such actual knowledge, there can be no reckless disregard. *See, e.g., Saltz v. First Frontier, LP*, No. 10 Civ. 964 (LBS), 2010 WL 5298225, at *5, 8 (S.D.N.Y. Dec. 23, 2010) (finding red flag allegations relating to Madoff insufficient to establish recklessness or gross negligence where "Plaintiffs offer no evidence Defendants were aware of most red flags, and those of which Defendants were aware, were not so serious as to infer intent to defraud"). Also there is no meaningful particularization of facts that support a reasonable inference that a particular red flag posed a high risk that sham

transactions were actually occurring. Putative red flags that might establish negligence are not enough to establish a plausible allegation of scienter. *See* Joint Br. at 33-34.

11. The Herald Plaintiffs' civil conspiracy allegations, *see* HC Count 1, ¶¶ 647-50, fail because there is no plausible allegation that HSBC agreed to join any conspiracy.

12. The Thema Plaintiffs' claim for third party breach of contract fails because the Thema Complaint points to nothing in HSSI's and HTIE's service agreements with the Fund suggesting that investors were intended beneficiaries, but merely recites this element, *see* TC Count 16, ¶ 524, without any textual support.

13. Finally, the Herald Plaintiffs' conversion claim asserts that HSBC converted funds "through the unlawful 'investment' of [Plaintiffs'] funds," i.e., by transferring funds to a BLMIS bank account for the benefit of the Herald Funds. *See* HC Count 2, ¶¶ 636, 652-54. But Plaintiffs allege that each investor's funds were commingled and therefore cannot meet the requirement that the converted assets be "specifically identifiable." Joint Br. at 38-39. Moreover, Plaintiffs have not plausibly alleged that HSBC "intentionally and without authority," *see id.*, deprived their right to possession, as HSBC acted at the direction of the Funds under contractual authority when it sent funds to BLMIS.

14. Annexed hereto are true and correct copies of the following documents:

- | | |
|-----------------------|--|
| Exhibit 1 | Declaration of Deborah D'Aubney, dated June 28, 2011 |
| Exhibit 2 | Declaration of André Prüm, dated June 28, 2011 |
| Exhibit 3 | Declaration of Bill Shipsey, S.C., dated June 28, 2011 |
| Exhibit 4 | Declaration of Sharon Daly, dated June 28, 2011 |
| Exhibit 5 | Declaration of Mark Phillips, Q.C., dated June 28, 2011 |
| Exhibits 6-9 | Examples of Herald SPC, Herald (LUX) and Primeo Subscription Forms |
| Exhibits 10-11 | Excerpts of Offering Memoranda for Herald SPC and Primeo |

Executed on June 29, 2011, at New York, New York.

/s/ Evan A. Davis

EVAN A. DAVIS