FILED: NEW YORK COUNTY CLERK 05/11/2010 INDEX NO. 603750/2008
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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: MELVIN L. SCHWEITZER J.S.C. PART 45
Justice

Silver Oak Capital L.L.C., et al INDEX NO. 603750/08

MOTION DATE

-v-

UBS, A.G., et al. MOTION SEQ. NO. 005

MOTION CAL. NO.

The following papers, numbered 1 to ______ were read on this motion to/for ______

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion to dismiss is granted in part, and denied in part per the attached Decision and Order.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE FOR THE FOLLOWING REASON(S):

Dated: May 10, 2010

MELVIN L. SCHWEITZER J.S.C.

Check one: ☐ FINAL DISPOSITION ☑ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK : PART 45

SILVER OAK CAPITAL L.L.C., HFTP INVESTMENT L.L.C., PROMETHEAN I MASTER, LTD., f/k/a GAIA OFFSHORE MASTER INVESTMENT FUND, LTD., PROMETHEAN II MASTER L.P., PORTSIDE GROWTH AND OPPORTUNITY FUND,

Plaintiffs,

-against-

UBS, A.G., d/b/a UBS INVESTMENT BANK, UBS SECURITIES L.L.C., and UBS FINANCIAL SERVICES INC.,

Defendants.

Index No. 603750/08

DECISION AND ORDER

Motion Sequence No. 005

MELVIN L. SCHWEITZER, J.:

Background

Plaintiffs bring this action against defendants alleging common law fraud, aiding and abetting fraud, negligent misrepresentation and unjust enrichment in connection with their April 2006 $50 million investment in MediCor Ltd. (MediCor). Defendants move to dismiss the plaintiffs' amended complaint pursuant to CPLR 3211 (a) (7).

For purposes of this motion, the facts are assumed to be as alleged in plaintiffs' First Amended Complaint.

Plaintiffs are, respectively, a Cayman Islands corporation, a Cayman Islands limited partnership, a Cayman Islands exempted company and two Delaware limited liability companies which invested an aggregate of $50 million in MediCor, a company formed by Donald J. McGhan (Mr. McGhan) to develop and market medical devices.

Defendants UBS, A.G. (UBS), UBS Financial Services, Inc. (Financial) and UBS Securities L.L.C. (Securities) are affiliated financial institutions providing investment banking, securities and other financial services.

UBS is a corporation organized under the laws of Switzerland with its principal place of business in Zurich. Financial and Securities, respectively, are a corporation and a limited liability company, each organized under the laws of the State of Delaware and each with its principal place of business in New York. Each is a wholly-owned subsidiary of UBS. UBS Investment Bank is a nominal business group of UBS which operates in the United States through subsidiaries of UBS, including Securities and Financial.

In February 2006, each of the defendants assisted MediCor in marketing to plaintiffs $50 million aggregate principal amount of MediCor's senior secured convertible notes and warrants to purchase up to 3,125,000 shares of MediCor common stock at $4.50 per share for a purchase price of $50 million. In connection with the marketing activity, plaintiffs allege that Financial and Securities, "prepared and distributed or caused to be prepared and distributed, on behalf of UBS, A.G." to plaintiffs a Company Overview and a Private Placement Memorandum with respect to MediCor's business, financial condition and future prospects. Each of these marketing documents contained representations that MediCor had a strong management team led by Mr. McGhan and that Mr. McGhan and his affiliates had invested $17 million in equity and $58 million in additional capital in MediCor for operations and acquisitions. Additionally, a slide presentation was made to plaintiffs which stated that Mr. McGhan personally had substantial invested capital in MediCor. The slide presentation also provided a summary of prior investments by Mr. McGhan which indicated he had the resources to make his investment in MediCor.

The Company Overview was published on "UBS" letterhead and did not specify any particular corporation or business group as the disseminating party. The Private Placement Memorandum was published on "UBS Investment Bank" letterhead. The slide presentation was prepared and disseminated by Securities. Additionally, oral representations to the effect mentioned above were made to plaintiffs by Stewart Kesmodel (Mr. Kesmodel) identified as a Director of "UBS Capital Markets Group" and "UBS Private Equity Placement Group," nominal business groups of UBS, A.G.

Plaintiffs allege that the representations made regarding Mr. McGhan's leadership and invested capital in the marketing documents, slide presentation and also orally were false when made and that defendants knew this to be the case or were reckless in not so knowing.

In January 2007, the Federal Bureau of Investigation uncovered a fraudulent ponzi scheme operated by Mr. McGhan in connection with certain tax advantaged investment vehicles ("Exchange Entities"). Mr. McGhan's investment capital in MediCor referred to above actually was a portion of the proceeds from the Exchange Entities that were used in the ponzi scheme. He resigned as a Director and Chairman of MediCor, repudiated certain commitments to fund MediCor, plead guilty to four counts of wire fraud and was sentenced to 10 years in prison. MediCor was unable to raise additional investment capital and was forced to declare bankruptcy in June 2007, resulting in plaintiffs losing most or all of the value of their investment.

In March 2007, MediCor and Financial were sued in a class action in Nevada by victims of the ponzi scheme. Plaintiffs were not parties to that action. Financial settled all claims asserted against it and all the other UBS parties for $23 million. In connection with the settlement, the United States District Court for the District of Nevada entered a Bar Order which provides in pertinent part:

> No Person, whether or not a party to any of the Actions, shall be permitted to bring a claim against any of the Released Persons arising from the failure of the Exchanged [sic] Entities in any way based on, arising from, or referable to any alleged damages incurred or allegedly incurred by any Releasing Persons pertaining to or arising from, in any way, directly or indirectly, the failure of the Exchange Entities.

Defendants move to dismiss the complaint here on the grounds, *inter alia*, that: the Bar Order prevents plaintiffs from bringing the claims set out in this action; the fraud claim does not meet required standards with respect to specificity, and also fails to properly allege reliance, loss causation or scienter; the aiding and abetting claim does not properly allege scienter or substantial assistance; and the negligent misrepresentation and unjust enrichment claims are barred by New York's Martin Act, N.Y. Gen. Bus. L. § 352 *et seq.*

Discussion

CPLR 3211 (a), "Motion to dismiss cause of action," states that:

> "[a] party may move for judgment dismissing one or more causes of action asserted against him on the ground that:
>
> (7) the pleading fails to state a cause of action. . . ."

The standard for review on this motion is clear.

> "It is well settled that on a motion to dismiss a complaint for failure to state a cause of action, the complaint must be construed in the light most favorable to the plaintiff and all factual allegations must be accepted as true." (*Allianz Underwriters Ins. Co. v Landmark Ins. Co.*, 13 AD3d 172, 174 [1st Dept 2004]. "The sole criterion on a motion to dismiss is whether the pleading states a cause of action, and if from its four corners factual allegations are discerned which taken

together manifest any cause of action cognizable at law, a motion for dismissal will fail. (*Id.*)."

Although the court accepts well-plead factual allegations of a complaint as true and accords them every favorable inference in a motion to dismiss under CPLR 3211, allegations consisting of bare legal conclusions are not entitled to such consideration. *Wilson v Hochberg*, 245 AD2d 116 (1st Dept 1997).

Bar Order

Defendants contend that the Bar Order applies to plaintiffs and that plaintiffs actually petitioned the federal court in Nevada which issued the Bar Order for a ruling that they were outside its scope. Defendants contend the court there denied plaintiffs' petition for this relief and plaintiffs chose not to appeal that ruling, thus bringing them within the purview of the Bar Order.[1] Defendants thus assert, that "[i]n view of Plaintiffs' inclusion within the scope of the Bar Order, the only questions are whether Plaintiffs' claims 'arise from the failure of the Exchange Entities' and whether they are 'in any way . . . referable to any alleged damages incurred or allegedly incurred by any Releasing Persons. . . .'" Defendants' Memorandum of Law in Support of Their Motion to Dismiss The First Amended Complaint at 6. Defendants thus concede that even if plaintiffs are within the scope of the Bar Order, the court must answer both of those two questions in the affirmative in order to hold that application of the Bar Order precludes plaintiffs from bringing this action.

The court is of the opinion that the Bar Order does not prevent assertion of plaintiffs' claims here as such claims do not arise from the failure of the Exchange Entities.

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[1] Defendants also argue that plaintiffs are bound by the Bar Order nevertheless because they were unnamed parties to certain of the actions that appeared on a "List of Actions" whose parties are bound by the Bar Order.

As explained above, when the ponzi scheme which involved looting the Exchange Entities unraveled, a class action was brought in Nevada by the members of the Exchange Entities whose monies had been stolen. Defendant Financial was caught up in the action by virtue of having provided financial services to Mr. McGhan and certain entities controlled by him. Financial was alleged to have participated in the ponzi scheme, and ultimately it paid $23 million to settle the class action claims and obtain peace for all UBS entities from additional claims brought by parties damaged by the failure of the Exchange Entities. Plaintiffs were neither parties to the class action nor were they Releasing Persons under the settlement.

It is the opinion of the court that plaintiffs' claims are direct claims for damages against defendants which arise from the circumstances of plaintiffs' $50 million investment in MediCor, not damages "arising from the failure of the Exchanged [sic] Entities." Plaintiffs have brought the action here alleging that defendants made misrepresentations to them regarding the source of MediCor's finance capital and the strength of its management, and that they made their investment because they relied on these misrepresentations. Their case is based on the theory that the value of the MediCor securities they purchased was far less at the moment of their purchase than the purchase price they paid. They attribute this inflated value to defendants' misrepresentations, and they claim that the disparity – their loss – was incurred to a large extent at the date of MediCor's bankruptcy. The court agrees that plaintiffs' loss was due to the failure of MediCor, *not* the failure of the Exchange Entities.

The court has not found relevant judicial precedent addressing the definition of the term "arising from." Additionally, counsel for the parties, in their thorough, thoughtful papers submitted here, have not brought any such precedent to the attention of the court. Consequently, the court turns to the common definition of the word "arising." It is said that a consequence arises from another act or condition if it comes into being or results from such act or condition. Webster II New College Dictionary, Houghton Mifflin, 2001. Taking into account this definition, the court is persuaded by plaintiffs' reasoning that the claims of the Nevada class members arose out of, or resulted from, the failure of the Exchange Entities, while plaintiffs' claims, in contrast, arose out of, or resulted from, the failure of MediCor. In the court's view, plaintiffs argument that they are suing defendants because of their alleged misrepresentations is compelling. Plaintiffs assert they suffered a cognizable injury when they invested $50 million on April 26, 2006 because the value of the securities they purchased at that time actually was substantially less than the purchase price they paid, and that this injury ultimately was realized in the normal course of events.

A number of scenarios may be posited either to support or to undermine plaintiffs' theory of their damage or loss. MediCor might have become so successful that it would not have needed the stolen capital diverted to it, and the capital might have been returned to the Exchange Entities without ever having been noticed. Were this to have happened, the misrepresentations alleged here would not have resulted in a loss to plaintiffs, even if the Exchange Entities had failed in any event. Another possible scenario is that the capital diverted to MediCor might have been returned to the Exchange Entities, and they might not have failed at all (or at least not until a much later date). In such an event, MediCor might have found itself under capitalized regardless, because Mr. McGhan never invested what defendants had represented that he did, and Medicor still might have failed as a result. Under this latter scenario, the alleged misrepresentations surely would have resulted in plaintiffs' loss. Accordingly, however refined counsel's arguments may be in parsing the subtle distinctions in the structure of the Bar Order, the court is not persuaded that, absent the failure of the Exchange Entities, plaintiffs would not have suffered a cognizable injury. The latter example above certainly posits the contrary.

The court also notes the absence of the common term "relating to" immediately after the term "arising from" in the first clause of the Bar Order. As the Supreme Court noted in *Travelers Indemnity v Bailey*, 129 S. Ct. 2195, 2203 (2009), citing *Smith v United States*, 113 S. Ct. 2050 (1993), the term "in relation to" is expansive when contained in a statute or Bar Order. The court has found no precedent to such effect with respect to the term "arising from." While inclusion of the term "relating to" in the first clause of the Bar Order would not necessarily change the court's opinion here, its absence certainly underscores the court's decision that the Bar Order entered in the Nevada class action does not preclude plaintiffs from bringing this action.

Fraud Claim

Plaintiffs have brought actions for fraud against UBS, Financial and Securities, arguing that *each* was a knowing or reckless participant in disseminating misrepresentations with respect to MediCor's capitalization and management strength in connection with the private placement of $50 million of MediCor's securities to plaintiffs. In order to properly state a claim for fraud, the plaintiffs are required to allege as against each defendant, "a misrepresentation or a material omission of fact which was false and known to be false by defendants, made for the purpose of inducing the other party to rely upon it, justifiable reliance by the other party on the misrepresentation or material omission and injury." *Lama Holding Co. v Smith Barney Inc.*, 88 NY2d 413, 421 (NY 1966). Each of these elements must be supported by allegations in the complaint which also satisfy the specificity requirements of CPLR 3016 (b).

Defendants support their motion to dismiss by isolating each defendant's actions from those of the other defendants in an effort to demonstrate that plaintiffs have not met the pleading requirements referenced above, including the specificity requirement.

The court is of the opinion with respect to Financial, that plaintiffs have alleged with specificity that it was involved in, or at least was aware of, the ponzi scheme and that it prepared the marketing documents and distributed them to plaintiffs, or caused them to be prepared and distributed. Plaintiffs have alleged that at the time Financial was aware of the ponzi scheme, it also introduced MediCor to Securities with the knowledge that Securities would disseminate misrepresentations regarding MediCor to potential investors. These allegations clearly satisfy the specificity requirements of CPLR 3016 (b) with respect to the essential element of a fraud claim, that is, Financial's knowing involvement in misrepresentations of fact to the plaintiffs. The court notes that in circumstances similar to those here, false statements disseminated by a corporation that did not know the statements were false (such as Securities, here) were correctly attributed to an affiliated corporation which *was* aware of their falsity. *In re Alston SA Sec. Litig.*, 406 F Supp 2d 433 (SDNY 2005). In that case, the court said:

> "The Court notes that a contrary result would present the dilemma the court described in *Kidder Peabody* (citation omitted). '[H]olding a subsidiary immune from liability for statements communicated by its parent under these facts would lead to an anomalous result. A subsidiary could freely disseminate false information to the market through its parent, but investors relying on that information to their detriment would be left with no remedy: an action could not be brought against the subsidiary, and the parent would escape liability because it lacked scienter. This would lead to a result so bizarre that Congress could not have intended it.'"

Id. at 467, n 30 (citation omitted).

With respect to Securities and UBS, in contrast, the complaint here fails to allege with specificity that either of these entities was aware of the ponzi scheme or aware that the representations in the marketing documents with respect to MediCor's capitalization or management strength were false. There is no allegation that anyone employed by Financial disclosed the ponzi scheme or MediCor's true capitalization to anyone at Securities or UBS. As defendants correctly point out, corporate entities are presumptively separate and the knowledge of a fraud by one corporation, in this case Financial, will not be imputed to another affiliated corporation - here, UBS or Securities. *See Oei v Citibank, N.A.*, 957 F Supp 492, 519 (SDNY 1997).

Plaintiffs frequently allege that the representations here were known to be false or recklessly made by "defendants" or by "UBS defendants," thus attempting to sweep UBS and Securities into the same class as Financial. In one case, plaintiffs specifically point to UBS "representative," Mr. Kesmodel, and allege that he falsely stated to plaintiffs' representatives that Mr. McGhan and his affiliates had made a substantial investment in MediCor. Even in this instance, however, plaintiffs only state in conclusory fashion that Mr. Kesmodel's statement was known to be false or was recklessly made, without any specific allegations as to what Mr. Kesmodel knew in this regard. This clearly is inadequate to specifically state claims against UBS and Securities.

In an attempt to salvage the complaint as to UBS and Securities, plaintiffs have alleged that UBS and Securities personnel knew of the longstanding relationship Financial had with MediCor, and that they had "unique access" to Financial's books and records which, if examined, would have disclosed the ponzi scheme. Neither of these assertions is sufficient to satisfy the specificity requirements of CPLR 3016 (b) regarding knowing misrepresentations by UBS and Securities. The fact that UBS and Securities knew of Financial's relationship with MediCor does not support an inference that either of these entities knew of a fraudulent scheme, as they might if they, themselves, had been one of the actual parties to that relationship. Nor does their access to information at Financial or their failure to adequately execute their due diligence responsibilities equate with a knowing participation in a fraud. *In Re Bayou Hedge Fund Litig.*, 534 F Supp 2d 405 (S.D.N.Y. 2007), *affd, South Cherry Street LLC v Hennesee Group LLC*, 573 F3d 98 (2d Cir 2009). Plaintiffs are left only with conclusory allegations that UBS and Securities knowingly or recklessly made the misrepresentations in the marketing materials, or orally. These are not sufficiently specific, and the fraud complaint against UBS and Securities is fatally flawed in this respect.

In reaching this conclusion, the court has considered plaintiffs' position and cited cases to the effect that in an analysis of a complex, pervasive fraud, knowledge of that fraud may be *inferred* from the circumstances in which it occurred. *See Pludeman v Northern Leasing Sys. Inc.*, 10 NY3d 486 (2008); *Houbigant Inc. v DeLoitte & Touche, LLP*, 303 AD2d 92 (1st Dept 2003). The facts of those cases are readily distinguished from those set forth in plaintiffs' complaint here. In *Pludeman*, knowledge of the fraud was found to have been sufficiently alleged against a company's top management where the fraud concerned a core business of the company, and where the defendants were officers who actually operated that business day-to-day in which the fraud was both pervasive and had taken place over many years. *Houbigant* involved an accounting malpractice claim where the issue was whether an accounting firm could have certified financial statements without having known of fraud in the particular circumstances. In contrast, inferring knowledge that misrepresentations were made here cannot be predicated on UBS' or Securities involvement in a long-running, pervasive scheme, and they certainly are not alleged to have been participants in a matter involving the intricacies of auditors liability. The cases cited by plaintiffs are thus of limited applicability to what is before the court and do not adequately support plaintiffs' argument in this regard.

Plaintiffs also argue "under familiar principles of '*respondeat superior*'" that defendant UBS, the Swiss parent of its affiliated U.S. financial institutions, Financial and Securities, is responsible for the actions taken by these subsidiaries, allegedly "on behalf of" UBS' business group division, "UBS Investment Bank." Plaintiffs' Memorandum in Opposition to Defendants' Motion to Dismiss the First Amended Complaint at 20. The fallacy in plaintiffs' reasoning is that the facts plead here are insufficient to allege a principal-agent relationship between UBS and either of these two subsidiaries. According to the complaint, each of these companies is a separately incorporated entity. That they also may be affiliated with nominal business group divisions that are not jural entities recognized by law, e.g. UBS Investment Bank, "through which" the parent does U.S. business, does not make them agents of the parent that conceived of them. The terms "group" or "division," whether used for marketing or internal identification purposes, simply do not alter the fundamental principles of corporate or agency law as they relate to a corporate parent and its subsidiaries.

For example, it is only by a registered broker dealer that UBS, by law, may carry out its private placement activities in the U.S., such as the sale of the MediCor securities to plaintiffs. And as defendants have pointed, it is UBS' subsidiary, Securities, which satisfied this legal requirement here and thus was able to act as placement agent for the offering. That a document entitled "Company Overview" was disseminated on a "UBS" letterhead, and that a "UBS Investment Bank" letterhead was used for the Private Placement Memorandum, does nothing to establish a principal-agent relationship between UBS and its broker-dealer subsidiary, Securities. Indeed, the individuals identified in the complaint as having been involved in the marketing of this offering were employed by either Securities or Financial, not UBS or a business grouping nominally used by UBS. Both Mr. Kesmodel and Mr. Robinson are specifically identified in the Private Placement Memorandum (Exhibit B to the Complaint) as employees of Securities.

Plaintiffs cite *Marine Midland Bank v John E. Russo Produce Co., Inc.*, 50 NY2d 31, 44 (1980) ("A principal that accepts the benefits of its agent's misdeeds is estopped to deny knowledge of the facts of which the agent was aware.") (citation omitted). The Court of Appeals, while reaffirming that an agent's scienter ordinarily will not be imputed to her corporate principal where she is deemed to have an interest adverse to her principal, held that knowledge may be imputed, however, where the relationship between the agent and the principal is so close that issues of fact necessarily are raised as to whether the agent *was* acting in the interests of her principal. There, two corporations were related by both blood and business, and both were sued for fraud and conversion in a check kiting scheme. The agent was a part-time bookkeeper for a wholesale and retail produce corporation owned by her sons. At the same time, this mother, together with her husband, were the sole shareholders of another corporation in the produce business which shared common offices and produce storage space, and conducted inter-company business with their sons' business. But central to the court's holding that the mother's knowledge of the scheme might be capable of imputation to her sons' company is that the mother was, in fact, an agent of the company as an employed part-time bookkeeper. There, the principal-agent relationship existed in fact and in law, so that the agent's knowledge could be imputed to her principal, if ultimately it were found to be warranted. Here, in contrast, as discussed above, nowhere does the UBS corporate structure involve an agency relationship between the UBS subsidiaries (and their respective employees) *viz*. the Swiss parent. There simply is no parallel between the cases and plaintiffs' reliance on the *Marine Midland Bank* decision is misplaced.

Defendants also argue that plaintiffs have not established reasonable reliance because the Placement Memorandum specifically instructed them to conduct their own due diligence, stated that UBS assumed no responsibility for checking the information in the Memorandum, and flatly stated that UBS made no representation as to the accuracy of information in it. While such disclaimers may act to negate liability for inaccurate information in some circumstances, here plaintiffs have alleged that Financial was fully aware that the representations as to capitalization and management strength were blatantly false when made. In such circumstances, disclaimers do not act effectively to undermine allegations of fraud, at least at the pleading stage. *Ackerman v Price Waterhouse*, 252 AD2d 179 (1st Dept.1998); *see also CP Kelco U.S., Inc. v Pharmacia Corp.*, 2002 WL 31230816 (D. Del 2002). If plaintiffs are correct, the disclaimer here cannot vitiate the fraud; rather, it is in fact part of the fraud.

Also, the disclaimers here were general, and not specific to the representations made with respect to MediCor's capitalization or management strength. As such, at the pleading stage, the disclaimers do not undermine plaintiffs' claim of justifiable reliance on such misrepresentations. *Steinhardt Group, Inc. v Citicorp*, 272 AD2d 255, 257 (1st Dept 2002). Finally, the alleged misstatements relate to facts peculiarly within Financial's knowledge. It is unlikely that plaintiffs pre-acquisition due diligence, no matter how thorough, would have discovered the actual situation with respect to MediCor's capitalization. Even Securities has asserted on this motion that it was not aware of the true state of affairs. Disclaimers generally are ineffective to defeat reliance claims in these situations, and certainly they do not do so with regard to this motion.

Next, defendants argue that plaintiffs have not properly plead scienter with respect to UBS and Securities, an essential element of fraud. This is a variant on their position that knowing misrepresentation has not been plead with sufficient specificity. Defendants assert that plaintiffs cannot clearly identify the persons acting for Securities in its marketing role who also were acting for Financial, and who thus were allegedly aware of the ponzi scheme. As noted above, there is no allegation that anyone at Financial communicated their knowledge of the ponzi scheme to anyone at UBS or Securities. The test for properly pleading scienter under New York law is that a plaintiff must identify "some rational basis for inferring that the alleged misrepresentation was knowingly made." *Houbigant Inc. v Deloitte & Touche LLP*, 303 AD2d 92, 98 (1st Dept 2003). Here, plaintiffs have done so repeatedly with respect to the scienter of Financial, but not of UBS or Securities.

Finally, with respect to plaintiffs' fraud claim, defendants argue that plaintiffs have not adequately plead loss causation. The court disagrees. Plaintiffs contend they were induced by fraudulent misrepresentations pertaining to MediCor's capitalization and strength of management to pay $50 million for securities worth far less than that amount. Plaintiffs assert they were damaged at the time of their investment and that their loss became known when the ponzi scheme unraveled. MediCor's reputation as a business entity was shattered, it lost access to the capital markets, and ultimately sought bankruptcy protection.

Plaintiffs call attention to *Stutman v Chem. Bank*, 95 NY2d 24 (2000) and *Sterling Nat'l Bank v Ernst & Young, LLP*, 2005 WL 3076341 (Sup Ct NY County, January 7, 2005) for the point that loss causation is established when it is reasonably foreseeable that a pecuniary loss will result from reliance on a misrepresentation. Their point is well taken. Here it was reasonably foreseeable that plaintiffs would lose most or all of their investment as a result of relying on the misrepresentations. Plaintiffs cite Justice Cahn's reasoning in *Sterling* to support their position. There, he said:

> "Defendants' representations gave the impression that Allied Deals was a bona fide business, when in fact Allied Deals was a criminal enterprise that had little or no actual business from its inception. Had defendants' audit fairly represented its financial condition, it would be evident that Allied Deals would never have been able to repay a loan. . . . Thus, it is foreseeable that Sterling would suffer losses once it was induced by defendants' representation to transact with Allied Deals. . . .It is a foreseeable result that Allied Deals would default on its loans when its true financial condition became known." 2005 WL 3076341 *6 (footnote omitted).

The alleged misrepresentations here gave the impression that MediCor was a bona fide, well capitalized business, not an entity financed by a ponzi scheme. It was foreseeable that plaintiffs would suffer severe losses once they were induced to invest in MediCor. The fact that Mr. McGhan apparently planned for MediCor to earn its way out of the untenable position in which it had been placed does not detract from this analysis. Finally, defendants' argument that plaintiffs lost their investment as a result of any number of unrelated reasons, such as the business failing to capture sufficient market share, is not persuasive at this stage of the proceedings. The court finds plaintiffs have adequately plead loss causation.

Aiding and Abetting

Under New York law, aiding and abetting requires the pleading of (i) a primary fraud, (ii) actual knowledge of the primary fraud, and (iii) substantial assistance with respect to implementation of the fraudulent scheme. The complaint clearly sets forth allegations necessary to state a claim for aiding and abetting fraudulent conduct against Financial but not as against UBS or Securities. Given the court's conclusions with regard to plaintiffs' claim of fraud, this result as pertains to the aiding and abetting claim is axiomatic. Plaintiffs have made allegations of fraud by Mr. McGhan, and have alleged Financial's actual knowledge of that fraud, as well as Financial's substantial assistance in the fraudulent activity. Defendants' arguments regarding these allegations as against Financial are thus subject to the same infirmities as with regard to the fraud allegation against Financial. As to UBS and Securities, however, there is no specific allegation of their actual knowledge of the fraudulent scheme and, consequently, the aiding and abetting claim against each of these entities is not adequately pled.

Negligent Misrepresentation and Unjust Enrichment

Defendants contend that both plaintiffs' claims for negligent misrepresentation and for unjust enrichment are barred by The Martin Act, New York General Business Law Art. 23-A, § 352 *et seq.* In *Jana Master Fund, Ltd. v JPMorgan Chase & Co.*, 2008 WL 746540 (Sup Ct, NY County 2008), Justice Fried carefully addressed the ambit of the Martin Act. He said:

> "The Martin Act, New York General Business Law Art. 23-A, § 352, *et seq.*, provides a further ground for dismissal of the claims for negligent misrepresentation. . . .The Martin Act prohibits various deceitful practices in the distribution, exchange, sale and purchase of securities which do not involve proof of scienter, and confers exclusive jurisdiction on the state's Attorney General to regulate and enforce its provisions. GBL § 352-c (1). There is no implied private right of action under the Martin Act. . . .Thus, the Act bars private common-law

> claims where the facts alleged would provide the Attorney General with grounds for instituting an action."
>
> "Claims for negligent misrepresentation . . . in connection with the purchase and sale of securities have been found to be barred by the Martin Act. *See Horn v 440 East 57th Co.*, 151 AD2d 112, 547 NYS2d 1 (1st Dept 1989). Here, the claims for negligent misrepresentation . . . allege that the defendants negligently misrepresented and concealed material from unspecified original note purchasers regarding Gwalia's true financial condition, inducing the note purchasers to enter into the purchases, and that defendants facilitated the issuance of the notes even though they knew the true state of Gwalia's finances. These claims clearly fall within the purview of the Martin Act, and are, therefore, dismissed." 2008 WL 746540 *5 (citations omitted).

The court is in agreement with the reasoning of *Jana*. Accordingly, plaintiffs' claim for negligent misrepresentation is dismissed.

Similarly, plaintiffs' common law claim of unjust enrichment, which in this case is based on alleged deceitful practices in connection with the sale of securities, also is dismissed, consistent with the holding in *Jana*.

Conclusion

Accordingly, it is

ORDERED that the motion to dismiss the first and second causes of action against defendants UBS, A.G. and UBS Securities L.L.C. and the third and fourth causes of action against defendants UBS, A.G., UBS Financial Services Inc. and UBS Securities L.L.C. is granted; and it is further

ORDERED that the motion to dismiss the first and second causes of action against defendant UBS Financial Services Inc. is denied.

Dated: May 10, 2010

ENTER:

J.S.C.