Abu Dhabi Commercial Bank P.J.S.C. v Credit Suisse Sec. (USA) LLC.
2011 NY Slip Op 33863(U)
August 1, 2011
Sup Ct, New York County
Docket Number: 115417/2010
Judge: O. Peter Sherwood

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: O. PETER SHERWOOD PART 49
Justice

ABU DHABI COMMERCIAL BANK P.J.S.C.,

Plaintiff,

-against-

CREDIT SUISSE SECURITIES (USA) LLC., ET. AL.,

Defendants.

INDEX NO. 115417/2010

MOTION DATE June 28, 2011

MOTION SEQ. NO. 001

MOTION CAL. NO. ______

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

	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 is decided in accordance with the accompanying decision and order.

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

Dated: August 1, 2011

O. PETER SHERWOOD, *J.S.C.*

Check one: ☑ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Check if appropriate: ☐ DO NOT POST ☐ REFERENCE

☐ SUBMIT ORDER/ JUDG. ☐ SETTLE ORDER/ JUDG.

[* 2]

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 49

---X

ABU DHABI COMMERCIAL BANK P.J.S.C.,

Plaintiff,

-against-

CREDIT SUISSE SECURITIES(USA) LLC,
CREDIT SUISSE INTERNATIONAL,
THE MCGRAW-HILL COMPANIES, INC.
(d/b/a STANDARD & POOR'S RATINGS SERVICES),

Defendants.

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DECISION AND ORDER

Index No. 115417/2010

Hon. O. Peter Sherwood, J.

This decision and order consolidates Motion Sequence Numbers 001 and 002 for disposition.

THE COMPLAINT

This action arises out of allegations that defendants Credit Suisse Securities (USA) LLC and Credit Suisse International (jointly, "Credit Suisse") and the McGraw-Hill Companies, Inc. d/b/a Standard & Poor's Rating Services ("S&P"), defrauded plaintiff Abu Dhabi Commercial Bank by making materially false statements and omissions to induce plaintiff into a restructuring transaction, causing plaintiff to lose a substantial portion of its original $40 million investment and face potential liability in excess of its investment. Presently before the court are motions by Credit Suisse (motion sequence number 001) and S&P (motion sequence number 002), to dismiss the complaint. For purposes of the motion, the allegations in the complaint must be taken as true.

Victoria Finance Ltd. ("Victoria") was a structured investment vehicle ("SIV") created in or about July 2002. Plaintiff held $40 million in Victoria's capital notes since 2005/2006 (complaint ¶ 3). Victoria was highly rated by S&P and Moody's until the financial markets began experiencing difficulties in late 2007 (*id*) Victoria's investment manager, non-party Ceres Capital Partners, LLC ("Ceres") proposed that it be restructured into what would become Farmington Financial Ltd ("Farmington"). Ceres and Credit Suisse allegedly represented that because Farmington's underlying assets would be identical to Victoria's but its debt would be long-term, the Farmington transaction would be able to bypass Victoria's liquidity issues (*id*). Plaintiff alleges that Credit Suisse and Ceres presented Farmington as a low-risk collateralized debt obligation ("CDO") and led plaintiff to believe that investing in it would salvage plaintiff's investment in Victoria (*id*). S&P is a nationally recognized statistical rating organization ("NRSRO") that issued an opinion as to the creditworthiness of Farmington. Plaintiff alleges that its decision to enter into the transaction hinged on S&P's rating of Farmington's credit (complaint ¶ 34-41).

Plaintiff agreed to the transaction and on November 23, 2007 exchanged its Victoria capital notes for Farmington capital notes (*id* ¶ 8). Credit Suisse made a term loan of $347 million to Farmington to purchase Victoria senior debt and plaintiff, along with other Farmington investors, assumed the risk of a credit default swap ("CDS"), extending credit protection to Credit Suisse for the term loan (*id*). Plaintiff alleges that Credit Suisse purchased the Victoria senior debt from itself and its clients rather than on the open market in order to get that "toxic" debt off its books at higher than market prices and to inflate the principal amount of the loan to Farmington. This was contrary to plaintiff's understanding that Credit Suisse would engage in arms-length third-party negotiations to purchase Victoria's senior debt at favorable prices and therefore was fraudulent (*id* ¶ 8). Plaintiff argues that the Farmington transaction resulted in it suffering a substantial loss on its $40 million investment and facing potential liability for the difference between the notional value of the CDS and the deteriorated value of the underlying assets (*id* ¶ 10).

The complaint alleges the following causes of action against all defendants: (1) common law fraud, (2) fraudulent inducement, (3) fraudulent concealment, (4) aiding and abetting each others' fraud, (5) breach of fiduciary duty, (6) aiding and abetting breach of fiduciary duty, (7) negligent misrepresentation, and (8) unjust enrichment. Both Credit Suisse and S&P move to dismiss the complaint in its entirety.

DISCUSSION

I. Applicable Law

A. Fraud, fraudulent inducement and fraudulent concealment

To state a claim for fraud, plaintiff must allege with the particularity required by CPLR 3016(b), facts that demonstrate (1) a misrepresentation or concealment of a material fact by each defendant, (2) that it was made with knowledge of its falsity and an intent to defraud, (3) justifiable reliance on the deception by the plaintiff, and (4) resulting injury (*See Zannett Lombardier, Ltd. v Maslow*, 29 AD3d 495, 495-496 [1st Dept 2006]). To plead fraudulent inducement, plaintiff must satisfy the above requirements of common law fraud and further allege that the defendants intended to induce some party to act on the statement made by defendant. (*see GoSmile, Inc. v Levine*, 81 AD3d 77, 81 [1st Dept 2010]). Finally, fraudulent concealment requires "an allegation that the defendant had a duty to disclose material information and that it failed to do so." (*P. T. Bank Central Asia v ABN AMRO Bank N.V.*, 301 AD2d 373, 376 [1st Dept 2003]).

B. Breach of fiduciary duty

"To establish a breach of fiduciary duty, the plaintiff must show the existence of a fiduciary relationship, misconduct that induced the plaintiff to engage in the transaction in question, and damages directly caused by that misconduct." (*Barrett v Freifeld*, 64 AD3d 736, 739 [2d Dept 2009]). "A fiduciary relationship exists between two persons when one of them is under a duty to act for or to give advice for the benefit of another upon matters within the scope of the relation" (*AG Capital Funding Partners, L.P. v State St. Bank & Trust Co.*, 11 N.Y.3d 146, 158 [2008]) "in an arm's-length business transaction involving sophisticated business people." (*Barrett* at 739).

C. Aiding and abetting causes of action

"In order to plead properly a claim for aiding and abetting fraud, the complaint must allege (1) the existence of an underlying fraud; (2) knowledge of the fraud on the part of the aider and abettor; and (3) substantial assistance by the aider and abettor in achievement of the fraud." (*Stanfield Offshore Leveraged Assets, Ltd. v Metro. Life Ins. Co.*, 64 AD3d 472, 475 [1st Dept 2009] [internal citations and quotation marks omitted]). A claim for aiding and abetting breach of fiduciary duty likewise requires "(1) a breach by a fiduciary of obligations to another, (2) that the defendant knowingly induced or participated in the breach, and (3) that plaintiff suffered damage as a result of the breach (*see Kaufman v Cohen*, 307 AD2d 113, 125 [1st Dept 2003]).

D. Negligent misrepresentation

Similarly, a cause of action for negligent misrepresentation arises only where there is a duty to give the correct information, knowledge or its equivalent that the information is desired for a serious purpose, that he to whom it is given intends to rely and act upon it, that if false or erroneous he will because of it be injured in person or property, and the relationship of the parties must be such that the one has the right to rely upon the other for information, and the other giving the information owes a duty to give it with care (*see Eiseman v State of New York*, 70 NY2d 175, 187-188 [1987]). "[A] cause of action [for negligent misrepresentation] requires that the underlying relationship between the parties be one of contract or the bond between them so close as to be the functional equivalent of contractual privity." (*Ossining Union Free School Dist. v Anderson LaRocca Anderson*, 73 NY2d 417, 419 [1989]). More recently, the Court of Appeals stated that "before liability may attach, the evidence must demonstrate (1) an awareness by the maker of the statement that it is to be used for a particular purpose, (2) reliance by a known party on the statement in furtherance of that purpose, and (3) some conduct by the maker of the statement linking it to the relying party and evincing its understanding of that reliance." (*Parrott v Coopers & Lybrand, L.L.P.*, 95 NY2d 479, 484 [2000]).

E. Unjust enrichment

"To state a cause of action for unjust enrichment, a plaintiff must allege that it conferred a benefit upon the defendant, and that the defendant will obtain such benefit without adequately compensating plaintiff therefor." (*Nakamura v. Fujii,* 253 AD2d 387, 390 [1st Dept 1998]).

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II. **Credit Suisse's Motion to Dismiss**

On its motion, Credit Suisse seeks dismissal of the entire complaint against it pursuant to CPLR 3211(a)(1) (defense upon documentary evidence), CPLR 3211(a)(7) (failure to state a claim) and CPLR 3016(b) (failure to plead fraud with specificity).

A. Fraud, fraudulent inducement and concealment

In its complaint, plaintiff makes several conclusory statements regarding its communications with Credit Suisse in reliance on which it entered into the Farmington transaction and was defrauded by Credit Suisse. Documentary evidence reveals otherwise.

Plaintiff states that it was told that an investment in Farmington was "safe", "not risky" and would preserve plaintiff's capital. (*see* complaint ¶¶ 189[a]-[d]). However, the transaction documents present a different picture. Both the term sheet and subscription agreement state that "TRANSACTIONS DISCUSSED HEREIN INVOLVE A HIGH DEGREE OF RISK" (Smith Aff., Ex. E ("Term Sheet") at 3 [emphasis in the original]) including a risk of loss of all or a substantial part of its investment (Smith Aff., Ex. B ("Subscription Agreement") at ¶ 3[b]); that "A TOTAL LOSS OF YOUR INVESTMENT COULD OCCUR UNDER CERTAIN SCENARIOS" (Term Sheet at 3 [emphasis in the original]) and finally, "the Transaction will increase [plaintiff's] exposure to the Investment portfolio and its risk of loss by up to ten times the amount of its investment in ... [the] Capital Notes." (Subscription Agreement at ¶ 3[b]).

Plaintiff further alleges that "defendants falsely represented that Farmington's assets, term loan and capital notes were highly rated" (complaint, ¶ 9). However, according to documentary evidence, the term loan and the Senior Capital Notes were not yet rated, disclosures plaintiff acknowledged in the Subscription Agreement. (Subscription Agreement at ¶ 3[i] ["[plaintiff] understands the [Farmington] Capital Notes will not be rated as of the Closing Date and there is no assurance that the [Farmington] Capital Notes will be rated, or if rated, that such rating will be maintained."]). Plaintiff also acknowledged that the ratings on Victoria Capital Notes and the securities in the collateral were currently being reevaluated by the credit rating agencies which were then adjusting their rating methodologies, and that "such rating agencies have downgraded (or put on a watch list for possible downgrade) the senior debt obligations of [Victoria] [and] the Victoria capital notes." (Subscription Agreement at ¶ 3[g]). These disclaimers are summarized succinctly in the Term Sheet ("[n]o assurances can be made as to what ratings the Term Loan and Senior Capital Notes will receive or maintain, if any"). (Term Sheet at 7). Finally, plaintiff was told that all information pertaining to Victoria was obtained from Ceres, and that defendant Credit Suisse neither verified it nor made "any representations with respect to [its] accuracy, completeness or fairness." (Term Sheet at 2).

With regard to Farmington's underlying assets, plaintiff alleges, that it did not have "the credit quality that defendants represented in the Farmington selling documents." (complaint, ¶ 7). In fact, not only did Credit Suisse not make any representations concerning the underlying assets (*see*

Term Sheet at 46 ["the Refinancing Transactions will not improve the credit quality of the Investment portfolio underlying any investor's Victoria Capital Notes"]) but plaintiff was aware of this fact, since the transaction involved a "vertical slice"[1] of Victoria's assets and acknowledged it. (see Subscription Agreement ¶3[g][I], [iii].)

Finally, plaintiff's alleged general reliance on Credit Suisse was completely unreasonable given the numerous disclaimers inserted into the transaction documents, some dating as far back as September 2005: plaintiff "is not relying on any communication (written or oral) of [Credit Suisse] as investment advice or as a recommendation to enter into [the CDS]" (Smith Aff., Ex. D ("CDS Schedule" dated 9/28/2005) at 35); plaintiff "is not relying (for purposes of making any investment decision or otherwise) upon any advice, counsel or representations (whether written or oral) of the Company, Credit Suisse, the Capital Notes Issuing Agent, the Investment Manager or any of their respective affiliates (Subscription Agreement at ¶ 3[e][iv]), and that plaintiff "has consulted with its own legal, regulatory, tax, business, investment, financial, and accounting advisors to the extent that it has deemed necessary... and made its own investment decisions" (Subscription Agreement at ¶ 3[e][I]).

On the basis of the documentary evidence described above, the court concludes that plaintiff has failed to allege facts sufficient to satisfy the reliance prong of the fraud, fraudulent inducement and fraudulent concealment causes of action. These causes of action must be dismissed.

B. <u>Fraudulent concealment, negligent misrepresentation</u>

The causes of action for fraudulent concealment and negligent misrepresentation require a duty to disclose the correct information. Plaintiff argues that such a relationship giving rise to that a duty arose from defendants' "unique positions of control over the information necessary for [plaintiff] to make an informed decision concerning the transactions at issue.... As a result of their superior knowledge concerning the transactions at issue and the nature of their involvement in advising or otherwise assisting [plaintiff] in determining whether to invest in Farmington... defendants occupied positions of influence that gave rise to a duty to accurate disclose the misrepresented or omitted information." (complaint, ¶¶ 225, 226; see also ¶250).

Under New York law, in the context of an arm's length relationship, no such duty will be found (*see United Safety of Am. v Consolidated Edison Co.*, 213 AD2d 283, 286 [1st Dept 1995]). "[A] party's "unique or special expertise" alone is insufficient to create an issue of fact concerning

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[1]"Vertical slicing" in the context of an SIV is allocation "of a proportionate share of each asset in the SIV's portfolio, calculated according to their proportionate share of the SIV's liabilities." (Greg B. Cioffi and David H. Sagalyn, When In Doubt, "Vertical Slice" It?, Asset Securitization Report, Dec. 15, 2008, available at http://www.sewkis.com/files/Publication/1789c2f1-1806-40db-94f9-00753ebbb9c4/Presentation/PublicationAttachment/3c010b8d-bf2c-4e5e-8729-25f916add1c1/When%20In%20DoubtVertical%20SliceIt.pdf [accessed July 18, 2011].

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the existence of a special relationship (*see M&T Bank Corp. v Gemstone CDO VII, Ltd.*, 68 AD3d 1747, 1750 [4th Dept 2009] [citing *Kimmell v Schaefer*, 89 NY2d 257, 264 (1996)]). In *M&T Bank Corp.*, the court found that there was no special relationship "in light of the facts that...offering circulars contained the various limitations and disclaimers." *Id.*

Similarly here, the relationship between plaintiff and defendant Credit Suisse was arm's length, as disclosed to and acknowledged by plaintiff in the Subscription Agreement (*see* Section I.A. supra). Therefore, plaintiff failed to state a cause of action for fraudulent concealment and negligent misrepresentation and they must be dismissed.

C. Breach of fiduciary duty

As to the Fifth Cause of Action for breach of fiduciary duty, the claim is precluded by the terms of the Subscription Agreement, wherein plaintiff acknowledges that "none of the Company, the Capital Notes Issuing Agent, the Investment Manager, Credit Suisse or any of their respective affiliates is acting as a fiduciary or financial or investment advisor to the [plaintiff]." (Subscription Agreement at ¶ 3[e][iii]).

Where as here, a plaintiff specifically disavows any fiduciary relationship with the defendant, plaintiff's breach of fiduciary duty claim must fail as a matter of law (*see* e.g. *JPMorgan Chase Bank, N.A. v Controladora Comercial Mexicana S.A.B. De C.V.*, No. 603215/08. 2010 WL 4868142 [Sup Ct New York County 2010] [Bransten, J.S.C.]).

D. Unjust enrichment

In its Eighth Cause of Action, plaintiff asserts a claim of unjust enrichment. "The essential inquiry in any action for unjust enrichment or restitution is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered." (*Sperry v Crompton Corp.*, 8 NY3d 204, 215 [2007]). Further, "[a] claim for unjust enrichment does not lie to relieve a party of the consequences of the party's own failure to exercise caution with respect to a business transaction." (*Dragon Inv. Co. II LLC v Shanahan*, 49 AD3d 403, 405 [1st Dept 2008]). Moreover, "recovery for unjust enrichment is barred by a valid and enforceable contract." (*Whitman Realty Group, Inc. v Galano*, 41 AD3d 590, 593 [2d Dept 2007]).

Such is the situation here. Plaintiff had an arms length relationship akin to contract with defendant Credit Suisse, which precludes it from bringing an unjust enrichment cause of action against said defendant.

III. S&P's Motion to Dismiss

In motion sequence number 002, S&P moves to dismiss the entire complaint against it pursuant to CPLR 3211(a)(1) (defense upon documentary evidence) and CPLR 3211(a)(7) (failure to state a claim). The motion must be granted.

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A. Fraud and fraudulent inducement (1st and 2nd causes of action)

Plaintiff makes two types of allegations regarding S&P's alleged fraudulent conduct in this transaction. First, it argues that in rating Farmington, S&P assumed a "distinctly commercial role" for which it was paid "approximately three times the amount it received for rating traditional corporate or government bonds." (complaint ¶ 42). Plaintiff concludes that this created a conflict of interest, leading S&P to give higher ratings than warranted in order to maximize its compensation and ensure recurring business from investment banks, like Credit Suisse. (*Id.* ¶ 45). Second, plaintiff questions S&P's ratings methodology. It argues that the models and default inputs used by S&P were antiquated, and resulted in unjustifiably high credit ratings for the Farmington products. (complaint, ¶¶ 46-47, 134, 138-140).

Neither of these allegations rises to the level of conduct that would be sufficient to state a cause of action for fraud or fraudulent inducement. S&P's then-used and now-questioned compensation model was well known in the financial services industry and was readily discoverable by plaintiff with a modest measure of due diligence. Similarly, S&P's use of allegedly inferior rating methodology does not constitute fraud. Plaintiff does not, nor could it, allege that S&P used this methodology for the purposes of defrauding plaintiff alone.

Moreover, plaintiff's allegations of reliance are contradicted by the terms of transaction documents discussed at Section II.A above which disclosed that the Term Loan and the Capital Notes were not yet rated at the time of closing, and that Victoria's ratings were being reevaluated at the time and likely on a downwards trajectory (Subscription Agreement at ¶¶ 3[i], [g]; Term Sheet at 2, 7). Since plaintiff was willing to enter into the transaction before the notes and loan were rated, it could not have relied upon them in entering that transaction.

B. Fraudulent concealment, negligent misrepresentation (3rd, 7th causes of action)

The causes of action for fraudulent concealment and negligent misrepresentation require a duty to disclose the correct information. Plaintiff argues that a relationship giving rise to such a duty arose due to defendants' "unique positions of control over the information necessary for [plaintiff] to make an informed decision concerning the transactions at issue.... As a result of their superior knowledge concerning the transactions at issue and the nature of their involvement in advising or otherwise assisting [plaintiff] in determining whether to invest in Farmington... defendants occupied positions of influence that gave rise to a duty to accurate disclose the misrepresented or omitted information." (complaint, ¶¶ 225, 226; see also ¶ 250).

S&P argues that such a relationship didn't exist since the parties never even had contact with one another. Plaintiff counters that such a relationship did exist since S&P had unique and specialized expertise regarding this transaction and was in a special position of confidence and trust. *(see Kimmell*, 89 NY2d at 264). S&P distinguishes *Kimmel* on the grounds that the parties had several direct contacts, whereas here, there were no communications between the parties at all. Plaintiff's relationship with S&P fails to satisfy these indicia. Here, unlike in *Kimmel*, the parties did not have direct contact.

C. Breach of fiduciary duty (5th cause of action)

Plaintiff argues that "[t]he creation of a fiduciary duty does not depend upon the existence of an agreement or contract between the parties... ." (*Barrett*, 64 AD3d at 739). Plaintiff contends that "such a relationship may arise where, as here, one party reposes confidence in another and reasonably relies on the other's superior expertise or knowledge... ." (Plaintiff's Memorandum of Law at 17 [citing *Barrett, supra*]). Plaintiff ignores the remainder of the quote from *Barrett* where the court stated that an existence of "an arm's-length business transaction involving sophisticated business people" precludes finding of such a fiduciary duty (*id* at 739). Here, S&P's relationship was with co-defendant Credit Suisse. Plaintiff had no contact with S&P. Therefore, if any relationship existed, it was an arm's length business one, and not a special one creating fiduciary duty to plaintiff.

D. Unjust enrichment (8th cause of action)

As set out above, "[t]he essential inquiry in any action for unjust enrichment or restitution is whether it is against equity and good conscience to permit the defendant to retain what is sought to be recovered." (*Sperry*, 8 NY3d at 215). "While...a plaintiff need not be in privity with the defendant to state a claim for unjust enrichment,...a claim does not lie [when the relationship] is simply too attenuated". (*Edelman v. Starwood Capital Group, LLC*, 2008 WL 2713489 [Sup Ct New York County 2008] [Bransten, JSC]).

Such is the situation with regard to the relationship between plaintiff and defendant S&P. Plaintiff not only lacked contractual privity with the defendant, it failed to allege any contact between the two.

E. First Amendment and preemption

Defendant S&P also moves to dismiss some causes of action based on First Amendment and preemption grounds. Having found that plaintiff failed to state a cause of action against the defendant, the court need not reach these grounds.

III. **Both Defendants**

A. Aiding and abetting causes of action

In order to plead properly a claim for aiding and abetting fraud or breach of fiduciary duty, plaintiff must sufficiently plead the existence of the underlying tort (*see Nat'l Westminster Bank USA v Weksel*, 124 AD2d 144 [1st Dept 1987]; *Kaufman v. Cohen*, 307 AD2d 113, 125 [1st Dept 2003]).

Having failed to do so with regard to either defendant, the aiding and abetting causes of action are likewise dismissed.

Accordingly, it is

ORDERED that the motion of defendants Credit Suisse Securities (USA) LLC and Credit Suisse International to dismiss the complaint herein is GRANTED and the complaint is DISMISSED in its entirety as against said defendants, and the Clerk is directed to enter judgment together with costs accordingly in favor of said defendants; and it is further

ORDERED that the motion of defendant McGraw-Hill Companies, Inc. (d/b/a Standard & Poor's Ratings Services to dismiss the complaint herein is GRANTED and the complaint is DISMISSED in its entirety as against said defendant, and the Clerk is directed to enter judgment together with costs accordingly in favor of said defendant; and it is further

ORDERED that counsel for the moving parties shall serve a copy of this order with notice of entry upon the County Clerk (Room 300) and the clerk of the Trial Support Office (Room 158).

This constitutes the Decision and Order of the Court.

DATED: August 1, 2011

E N T E R:

O. P. Sherwood

O. PETER SHERWOOD, J.S.C.