Va Mgt., LP v Odeon Capital Group LLC
2020 NY Slip Op 31441(U)
April 29, 2020
Supreme Court, New York County
Docket Number: 654492/2019
Judge: Andrew Borrok

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: HON. ANDREW BORROK **PART** IAS MOTION 53EFM

Justice

----------X

VA MANAGEMENT, LP,

Plaintiff,

- v -

ODEON CAPITAL GROUP LLC, JANNEY MONTGOMERY SCOTT LLC,C&CO/PRINCERIDGE LLC,JVB FINANCIAL GROUP, LLC

Defendant.

----------X

INDEX NO. 654492/2019

MOTION DATE

MOTION SEQ. NO. 003 004 005

DECISION + ORDER ON MOTION

The following e-filed documents, listed by NYSCEF document number (Motion 003) 29, 30, 31, 32, 33, 34, 35, 36, 37, 38, 39, 52, 55, 56, 69, 70, 77

were read on this motion to/for DISMISS.

The following e-filed documents, listed by NYSCEF document number (Motion 004) 40, 41, 42, 43, 53, 71, 72, 76

were read on this motion to/for DISMISS.

The following e-filed documents, listed by NYSCEF document number (Motion 005) 44, 45, 46, 47, 48, 49, 50, 51, 54, 73, 74, 75

were read on this motion to/for DISMISS.

Upon the foregoing documents, the motions to dismiss of (i) Janney Montgomery Scott LLC's (**Janney**) (mtn. seq. no. 003) pursuant to CPLR 3211(a)(1), (a)(5) and (a)(7), (ii) Odeon Capital Group LLC's (**Odeon**) (mtn. seq. no. 004) pursuant to CPLR 3211 (a)(5) and (a)(7), and (iii) C&Co/PrinceRidge LLC (**PrinceRidge**) and JVB Financial Group, LLC's (**JVB**) (mtn. seq. no. 005) pursuant to CPLR 3211(a)(1), (a)(5) and (a)(7) are denied for the reasons set forth below.

THE RELEVANT FACTS AND CIRCUMSTANCES

VA Management LP was a registered investment advisor with approximately $8 billion of assets under management known as Visium Asset Management, LP (**Visium**) (Compl., ¶¶ 12-13). Visium alleges that Christophe Plaford, Stefan Lumiere, and Jason Thorell (i.e., certain non-party former employees referred to as the "Disloyal Insiders" in the Complaint) conspired with the defendants who are broker-dealers in an illegal securities marking scheme, causing Visium to have to liquidate its $8 billion in assets and destroying its business (*id.*, ¶¶ 14, 1). The Complaint alleges that the defendants "schemed with the Disloyal Insiders working for Visium to provide sham quotes for certain securities to the Disloyal Insiders, which quotes the Disloyal Insiders in turn provided to [Visium's] back office and outside administrator without revealing that the quotes were illegitimate" (*id.*, ¶ 2). At times, the defendants also allegedly provided the so-called "sham quotes" directly to Visium's back office and outside administrator to facilitate the mismarking scheme so as to increase the Disloyal Insiders' compensation and increase transaction revenues for the defendants (*id.*).

In order to make the sham quotes appear legitimate, the defendants and the Disloyal Insiders allegedly communicated about the specific desired sham prices, after which the defendants' employees emailed or instant messaged those prices back to Visium and/or the Disloyal Insiders as if they were the defendants' own legitimate quotes (*id.*, ¶ 3). The sham quotes had the effect of falsely inflating calculations of the values of certain securities held by Visium's funds, which, in turn, increased the performance-based compensation paid by Visium to the Disloyal Insiders (*id.*, ¶ 5). The defendants also allegedly enabled the Disloyal Insiders' mismarking scheme by participating in illegal "painting the tape" transactions wherein the Disloyal Insiders purchased additional quantities of a security in which a fund has an established position and the inflated

price would then be reported to a fund's accountant as a market value transaction, thereby temporarily increasing the value of the entire position in the security and creating the false appearance of gains (*id.*, ¶¶ 6, 59-60). The defendants allegedly benefited from this mismarking scheme through transaction revenues, the development of business opportunities, and by earing revenue on trades that were executed at inflated prices (*id.*, ¶ 7). Visium claims that throughout this time it was unaware of the mismarking scheme and only learned of it when government agencies began investigating the mismarking activities in 2013 (*id.*, ¶¶ 8-9). Because these investigations were then widely reported in the financial press, there was a rush of redemption requests from Visium clients, which caused Visium to have to liquidate its funds in response, allegedly destroying over a billion dollars in enterprise value and causing tens of millions of dollars in related legal and investigative fees (*id.*, ¶¶ 10-11).

The defendants in this action are all SEC-registered broker-dealers. Odeon is member of FINRA and NASDAQ. During the relevant time period, Odeon employed an individual named Matt O'Callaghan as a senior bank trader (*id.*, ¶¶ 15-16). Mr. O'Callaghan had previously been censured, fined and suspended by FINRA 2009 for 18 months for mismarking his corporate bond trading book at non-party RBC Capital Markets Corporation so as to improve his profit and loss totals, resulting in his firm reporting inaccurate prices for corporate bonds on its books and records (*id.*, ¶ 17). The Complaint alleges that in his capacity as senior bank loan trader, Mr. O'Callaghan provided over 20 sham broker quotes to the Disloyal Insiders in furtherance of their mismarking scheme (*id.*, ¶ 18).

Janney is also a member of FINRA as well as a subsidiary of the Penn Mutual Life Insurance Company (*id.*, ¶ 19). A Janney director of institutional credit sales, Jonathan Brook, allegedly provided at least 198 sham broker quotes in furtherance of the mismarking scheme (*id.*, ¶¶ 20-21).

C&Co/Princeridge LLC was also a member of FINRA, NASDAQ and also the NYSE, among others. In 2014, it was consolidated into JVB, which is how it currently carries out its business (*id.*, ¶ 22). During the relevant time period, it employed an individual named Scott Vandersnow as managing director and head of corporate credit. Mr. Vandersnow allegedly provided at least 169 sham quotes in furtherance of the mismarking scheme (*id.*, ¶ 24).

One of the funds managed by Visium was the Visium Credit Master Fund, Ltd., which had two feeder funds, the Visium Credit Opportunities Offshore Fund, Ltd. and the Visium Credit Opportunities Fund, LP (together, the **Credit Fund**) (*id.*, ¶ 26). Between 2009 and 2013, the Credit Fund raised hundreds of millions of dollars in investor capital, mainly from institutional and fund-of-funds investors, and at its peak in March of 2012, the Credit Fund has a net asset value (NAV) of approximately $471.5 million (*id.*, ¶ 27-28). Another fund, the Visium Balanced Master Fund, Ltd., which had two feeder funds, the Visium Balanced Offshore Fund, Ltd. and the Visium Balanced Fund, LP (together, the **Balanced Fund**, and with the Credit Fund, the **Funds**) had a peak NAV of $4 billion in August 2015 (*id.*, ¶¶ 29-30).

The Funds' investments included a number of securities that were "relatively illiquid and difficult to value" (*id.*, ¶ 31). Visium's Fund Administrator, Morgan Stanley Fund Services,

would verify Visium's valuations of its Funds and their holdings by either (i) using certain established public pricing sources such as Reuters and Mark-It, or (ii) allowing Visium to "override" internal pricing where appropriate if Visium had reason to believe that the price used by the Fund Administrator was inconsistent with fair value and there was factual support for another pricing (*id.*, ¶¶ 32-34). To provide support for such internal pricing, Visium's accounting department and its Fund Administrator were directed by to look to established industry pricing sources such as Bloomberg, however, when market prices for a security were not readily available, Visium would use an "alternative pricing methodology" such as independent pricing quotes from outside brokers (e.g., the defendants, here) (*id.*, ¶¶ 34-37). The Complaint asserts that the use of broker quotes to value illiquid securities is a common industry practice and that it is frequently "not feasible" to obtain more than one quote (*id.*, ¶ 35).

According to the Complaint, the Disloyal Insiders took advantage of this common practice with their mismarking scheme. Specifically, starting in June of 2011, Messrs. Plaford and Lumiere would meet to predetermine sham prices for certain relatively illiquid assets in the Funds (*id.*, ¶¶ 39-40). Together, they would create a list of sham prices reflecting where they wanted each security to be marked for month-end valuation purposes, at prices that were generally significantly higher than the price available from public price data for long positions held by Visium and lower for short positions (*id.*, ¶ 42). This would increase their personal compensation. However, to implement the scheme, the Disloyal Insiders needed outside brokers to provide sham quotes from their official corporate email address or messaging platforms, to give the quotes an appearance of legitimacy (*id.*, ¶¶ 43-44). And, among other reasons outlined in the Complaint, including the manner in which this market operates, inasmuch as these quotes

had the shroud of legitimacy, there was no reason to believe that these quotes were illegitimate. The Complaint alleges that the Disloyal Insiders utilized the defendants for this, specifically, Mr. Lumiere obtained sham quotes from PrinceRidge and Janney, and Mr. Thorell, another Disloyal Insider, obtained sham quotes from Odeon (*id.*, ¶ 45). The defendants, in turn, received increased business in exchange for supplying these purportedly sham quotes and benefitted from certain other informal business opportunities from the Disloyal Insiders (*id.*, ¶¶ 46-47).

Specifically, the Complaint alleges that at month's end the Disloyal Insiders would contact certain employees of the Defendants by personal cell phone or another private method intended to avoid detection and communicate the desired sham price quote which the employees would then "parrot back" by way of official corporate email accounts and messaging platform as legitimate quotes from the defendant brokers, giving the sham quotes the appearance of independence (*id.*, ¶ 49). At times, employees of the defendants purportedly submitted the sham quotes directly to Visium's accounting and valuation staff to aid in the mismarking scheme (*id.*, ¶ 51). Per the Complaint, the scheme allegedly continued through September of 2013. Based on evidence introduced by the United States government at Mr. Lumiere's federal trial, through December of 2012 (the time through which the Government conducted its analysis), each of the defendants provided a combined total of 387 sham quotes to Visium (*id.*, ¶¶ 56-57, n. 1).

In addition, as described above, the defendants and the Disloyal Insiders also allegedly engaged in an illegal practice called "painting the tape." For example, in March of 2012, Mr. Brook allegedly offered Mr. Lumiere $800,000 worth of China Medical 4% Bonds at a per-bond price in the "low 30s," but based on Mr. Lumiere's instructions, Mr. Brook then sold approximately

$784,000 worth of bonds out of Janney inventory to the Credit Fund for around $43.25 per bond (*id.*, ¶¶ 61-62). Mr. Lumiere, thus, paid a higher per bond price than originally offered so as to inflate the value of all of the Credit Fund's China Medical Holdings, which also resulted in a windfall for Janney (*id.*, ¶¶ 63-64).

Visium claims that it did not learn of these schemes until it was notified of the Government's investigation (*id.*, ¶¶ 65-73). As noted, the redemption requests triggered as a result of the investigation allegedly reached a level at which it was impractical for Visium to operate its funds and it was forced to begin liquidating in July 2016, as a result of which it claims at least $1 billion in enterprise value was destroyed (*id.*, ¶¶ 80-82). In 2018, Visium formally relinquished its securities registration and in May of 2018, it entered into a settlement (the **Settlement**) with the Securities and Exchange Commission under which it paid over $6.3 million to resolve claims relating to the mismarking scheme (*id., ¶¶* 83-84). Mr. Vandersnow, who entered into a non-prosecution agreement with the government, admitted at Mr. Lumiere's trial to being part of a scheme to provide sham quotes from 2011 to 2013 (*id.*, ¶¶ 86-87).

The Complaint asserts a single cause of action against all three defendants for aiding and abetting breach of fiduciary duty based on the defendants' role in providing sham quotes to the Disloyal Insiders.

DISCUSSION

I. Applicable Standards

On a motion to dismiss pursuant to CPLR 3211, the court must afford the pleading a liberal construction and accept the facts alleged in the complaint as true, accord the plaintiff the benefit of every possible favorable inference and determine only if the facts as alleged fit into any cognizable legal theory (*Leon v Martinez,* 84 NY2d 83 [1994]). Under CPLR 3211(a)(1), dismissal is only warranted if the documentary evidence submitted conclusively establishes a defense to the asserted claims as a matter of law (*id.*). Dismissal pursuant to CPLR § 3211(a)(5) is warranted where the cause of action is barred by the statute of limitations. Finally, under CPLR 3211(a)(7), the court must assess only whether the plaintiff has a cause of action and not whether the plaintiff has stated one.

A claim for aiding and abetting a breach of fiduciary duty requires (1) a breach of fiduciary obligations to another, (2) that the defendant knowingly induced or participated in the breach, and (3) that the plaintiff suffered damages as a result (*Kaufman v Cohen*, 307 AD2d 113 [1st Dept 2003]). To establish the knowing participation element, a plaintiff is not required to allege that the aider and abettor had an intent to harm, only that the defendant had actual knowledge of the breach of duty (*id.*).

In moving to dismiss the defendants argue that the claim against them should be dismissed (i) pursuant to the *in pari delicto* doctrine, and (ii) because it is untimely.

II. *In Pari Delicto* Doctrine and the Adverse Interest Exception

Under the common law doctrine of *in pari delicto*, a court may not intercede to resolve a dispute between two wrongdoers (*Kirschner v KPMG* LLP, 15 NY3d 446 [2010]; *Concord Capital Mgt.,*

LLC v Bank of Am., N.A., 102 AD3d 406 [1st Dept 2013]). The policy behind this doctrine serves two important purposes. First, denying access to judicial relief for an admitted wrongdoer discourages illegal conduct (*Kirschner*, 15 NY3d at 464). Second, and just as importantly, the doctrine avoids entangling the courts in disputes between wrongdoers:

> No court should be required to serve as paymaster of the wages of crime, or referee between thieves. Therefore, the law will not extent its aid to either of the parties or listen to their complaints against each other, but will leave them where their own acts have placed them

(*id.*, quoting *Stone v Freeman*, 298 NY 268, 271 [1948] [Desmond, J.]).

Traditional principles of agency play an important role in the *in pari delicto* analysis (*id.*). Applying traditional agency principals, acts of agents and the knowledge they acquire while acting within the scope of their authority are presumptively imputed to their principals (*id.*, citing *Henry v Allen*, 151 NY 1, 9 [1896]). A corporation, thus, "must bear the consequences when it commits fraud" through its agents, which as the Court of Appeals noted serves another important public policy purpose: to provide an "incentive for a principal to select honest agents and delegate duties with care" (*id.* at 466).

Pursuant to the adverse interest exception, however, the acts of a corporate agent will not be imputed to the corporation as principal where the agent has completely abandoned his or her principal's interests and is acting entirely for his or her own benefit or for the benefit of a third-party (*id.* at 466-67). This exception to the general rule is narrowly applied in cases of outright theft, looting or embezzlement, i.e., "where the fraud is committed ***against*** a corporation rather than on its behalf" (*id.* at 467 [emphasis in original]). In cases of mixed motive, where the agent acts for both himself and the principal, however, application of the exception is precluded.

On the instant motions, the defendants argue that Visium's claim is barred pursuant to the doctrine of *in pari delicto* because the Complaint expressly admits that Visium's own employees engaged in criminal and fraudulent acts, that Mr. Plaford pleaded guilty to participating in the fraud, Mr. Lumiere was convicted, following a six-day trial, of wire fraud, securities fraud and conspiracy to commit those offenses, and that Mr. Thorell was described by the presiding federal judge as a "participant" in the illegal scheme (Compl., ¶ 14). In addition, the defendants argue that Visium, in fact, benefited from the scheme in that they collected asset management fees based on the inflated values. Under these circumstances, they argue, there can be no dispute that the actions of the Disloyal Insiders are imputed to Visium, thus barring Visium's claim against the defendants. The defendants also maintain that the adverse interest exception is inapplicable here because to come within the exception, the agent must have "totally abandoned his principal's interests" and acted entirely for his own or another's purposes (citing *Kirschner,* 15 NY3d at 466). The defendants argue that any harm suffered by Visium from the discovery of the fraud – rather than from the fraud itself – does not bear on whether the adverse interest exception applies. In other words, the defendants maintain that the Disloyal Insiders did not act ***against*** Visium simply because their conduct allegedly caused it to lose up to a billion dollars because that loss result only from the discovery of the fraud, and otherwise may have actually benefited the company. The argument fails.

As Visium argues in its opposition papers, the allegations are that the Disloyal Insiders acted not to benefit Visium, but to benefit themselves and that any benefit that Visium received was tangential and overshadowed by the harm that was created by the Disloyal Insiders' conduct.

And, viewing the facts alleged in the light most favorable to the plaintiff as the court must at this stage of the pleadings, there, at a bare minimum, exists factual issues as to whether Visium was the victim or the beneficiary of the Disloyal Insiders' fraud precluding dismissal on the pleadings based on the *in pari delicto* doctrine (*id.*, *Whitney Group LLC v Hunt-Scanlon Corp.*, 106 AD3d 671 [1st Dept 2013]; *Conway v Marcum & Kliegman LLP*, 176 AD3d 477 [1st Dept 2019] [reversing trial court dismissal where "plaintiffs raised issues of fact as to the adverse nature of their interests *vis-à-vis* those of their agents, the funds investment managers"]). Accordingly, the motion to dismiss based on the *in pari delicto* doctrine is denied.

III. Statute of Limitations

The applicable statute of limitations for fiduciary duty claims may be either six years or three years depending on the type of relief sought (CPLR §§ 213[1]; 214[4]). Where the relief sough is equitable in nature, a six-year statute of limitations applies. Where the suit only seeks money damages, a three-year statute of limitations for actions alleging "injury to property" applies.

Here, the defendants argue that Visium's claim is untimely even assuming the longer six year statute of limitations as the Complaint alleges that the mismarking scheme began in June of 2011 and, thus, the statute of limitations period expired in 2017. The defendants argue that Visium's subsequent filing of this action in August 2019, two years after the expiration of the six-year limitations period, renders the action untimely.

As an initial matter, although the Complaint seeks money damages, it also seeks disgorgement, which is an equitable remedy (*Chauffeurs, Local No. 391 v Terry*, 494 US 558, 571 [1990]). Therefore, the court will analyze the claim under the longer six-year limitations period. The six-year period is also appropriate here as the claim here sounds in fraud, which is governed by a six-year limitations period, as Visium correctly points out.

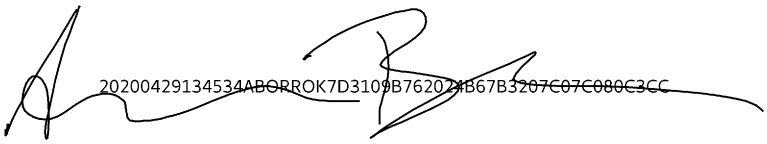
More significantly, the defendants incorrectly assume that the accrual date for the claim here was the ***beginning*** of the wrongful conduct. However, the Complaint alleges – and the defendants do not dispute – that the Conduct was not discovered until 2013, at which point Visium terminated the Disloyal Insiders' employment. Here, too, there appears to be a factual dispute. Visium posits that it did not ultimately discover the full extent of the fraud until December of 2019, when Mr. Plaford, the most senior of the Disloyal Insiders, had his employment terminated (Compl., ¶ 72). The defendants urge the court to apply an earlier date of April 2013, when Mr. Lumiere was terminated. However, it is unclear from the record what Visium knew of the fraud at that juncture. In this regard, the defendants rely on the opinion of the Hon. Jed Rakoff, who rendered the opinion in Mr. Lumiere's criminal case and noted that the mismarking scheme began to fall apart when "suspicion arose, and in April 2013, Lumiere was ***fired for poor performance***" (*United States v Lumiere*, 249 F Supp 3d 748, 754 [SD NY 2017] [emphasis added]). However, the mere fact that Mr. Lumiere was fired for poor performance does not permit the court to assume on a motion to dismiss that Visium had knowledge of the mismarking scheme. Likewise, the defendants cannot rely on trial testimony adduced in Mr. Lumiere's trial to resolve this issue as trial testimony is not documentary evidence within the meaning of CPLR 3211(a)(1) (*Attias v Costiera*, 120 AD3d 1281, 1282 [2d Dept 2014]). The Complaint pleads the

alleged breach continued through Mr. Plaford's termination in December of 2013 (*id.*, ¶¶ 71-73). Notably, the defendants took no action to repudiate, withdraw, or report the scheme before that time. Under the circumstances, the Complaint is sufficient to withstand a motion to dismiss.

Accordingly, it is

ORDERED that the defendants' motions to dismiss (seq. nos. 003-005) are denied, and it is further

ORDERED that the defendants are directed to serve an answer within 30 days of the date of this decision and order.



4/29/2020
DATE

ANDREW BORROK, J.S.C.

CHECK ONE:		CASE DISPOSED		X	NON-FINAL DISPOSITION		
		GRANTED	X DENIED		GRANTED IN PART		OTHER
APPLICATION:		SETTLE ORDER			SUBMIT ORDER		
CHECK IF APPROPRIATE:		INCLUDES TRANSFER/REASSIGN			FIDUCIARY APPOINTMENT		REFERENCE