McCormack Family Charitable Found. v Fidelity Brokerage Servs., LLC

2020 NY Slip Op 35613(U)

May 19, 2020

Supreme Court, New York County

Docket Number: Index No. 655270/2018

Judge: O. Peter Sherwood

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SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: COMMERCIAL DIVISION PART 49
- X
THE MCCORMACK FAMILY CHARITABLE FOUNDATION; WEEKAPAUG PARTNERS; OREGON-WINTER PARTNERS, LLC; CAMERON F. MACRAE III AND ANN B. MACRAE, INDIVIDUALLY; CAMERON F. MACRAE III AS TRUSTEE OF THE ART IV GST EXEMPT TRUST U/W/O CAMERON F. MACRAE; JAMES JOHNSON; BMC TRUST LLC; SMWC, INC.; OWC 12/23/67 TRUST FBO SAMUEL M. W. CASPERSEN; and THE OW CASPERSEN FOUNDATION FOR HEALTH & EDUCATION, INC.,

Plaintiffs,

-against-

FIDELITY BROKERAGE SERVICES, LLC; INTERACTIVE BROKERS, LLC; VISTA COINVEST, LLC; WINTER STREET, LLC; and IRV1NG PLACE III SPV LLC,

Defendants.
- X

DECISION AND ORDER
Index No.: 655270/2018

Motion Seq. Nos.: 001-002

O. PETER SHERWOOD, J.:

Motions number 001 and 002 are consolidated for disposition.

Plaintiffs claim they lost $8.28 million through the fraudulent actions of nonparty Andrew Caspersen. Defendants, brokerage firms Fidelity Brokerage Services, LLC (Fidelity) (motion sequence number 001) and Interactive Brokers LLC (Interactive, and together with Fidelity, the Brokers) (motion sequence number 002), move to dismiss the complaint pursuant to CPLR 3211(a)(7), arguing a failure to state a claim for which relief can be granted.

From 2003 through March 2013, Caspersen was employed by first one and then another brokerage firm. He was a managing principal at the second firm. From March 2013 until he was arrested by federal authorities in March 2016, Caspersen was registered with the Financial Industry Regulatory Authority (FINRA) as a licensed securities broker. Caspersen formed several companies, which plaintiffs call shell entities, and convinced plaintiffs and others to enter into promissory notes with the shell entities. Caspersen raised $38 million. He told plaintiffs

and others he would invest the funds raised through the promissory notes in a practically riskless debt instrument, which would generate interest of 15% to 20%.

Plaintiffs allege the shell entities never engaged in any business other than entering into the fraudulent promissory notes. "Caspersen suffered from a compulsive gambling addiction which compelled him to engage in the excessive and risky trading of options" (complaint, ¶ 41). In 2014-2015, Caspersen deposited the $38 million invested into the shell entities' accounts at the Bank of America (BOA). He then transferred those funds into the margin account he had maintained at Fidelity since 2008 and proceeded to lose $27 million on the stock market. On December 4, 2015, two days after Fidelity informed him it was shutting down his account, Caspersen wired $9.5 million from his Fidelity account to his newly opened, but not his first, margin account at Interactive. By the first week in March 2016, all of that money had been lost in the stock market. In July 2016, Caspersen pled guilty in the United Stated District Court, Southern District of New York to committing securities fraud and wire fraud "arising out of his theft of more than $38 million from friends, family and foundations" (*id.*, ¶ 52). He also stated he gambled away $20 million of his own money.

Plaintiffs allege the transfers from the shell entities' accounts to Fidelity and from Fidelity to Interactive were fraudulent conveyances under Debtor and Creditor Law (DCL) §§ 273-278. Plaintiffs seek to recover the transferred funds from the Brokers. Failing that, plaintiffs seek damages.

The complaint alleges the Brokers earned millions in commissions from Caspersen's stock market activity and exercised considerable control over the funds in his accounts. Under its customer agreement, each Broker could use the customer's funds to protect itself from risks associated with the customer's trading. For instance, the Brokers had the ability to liquidate securities without notice to the customer in order to ensure that the customer account satisfied minimum maintenance requirements.

The complaint includes allegations about Caspersen's Fidelity account, before he began, in 2014, to use it to accomplish the fraud. In July 2011, Fidelity made notations about the money laundering risk concerns presented by Caspersen's wiring of $3 million from a corporate entity that he controlled to his Fidelity account. In 2012, Caspersen lost approximately $6 million through trading at Fidelity, executing more than 40,000 trades. In 2015, when Caspersen was handling the funds invested by plaintiffs in the shell entities, his "trading escalate[d] out of

control" and he executed trades at a rate equal to or higher than 40,000 a year, until he lost $27 million of investor funds that year (complaint, ¶ 84). Caspersen executed each option trade by personally telephoning a Fidelity trader, placing multiple trades per day.

The complaint does not clarify whether the following allegations relate to the shell entities or previous financial dealings by Caspersen. The gist of the allegations is that the Fidelity traders knew Caspersen had a pattern of extensive trading that was highly inconsistent with activity expected in personal retail accounts. Fidelity's records show its awareness of Caspersen's "aberrant trading" (complaint, ¶ 88). Fidelity sent more than 10 letters to Caspersen warning that if he did not acknowledge in writing his sole responsibility for the escalating losses in his account, Fidelity would shut it down. Fidelity continuously warned Caspersen his account would be frozen if he did not satisfy pending margin calls with cash as opposed to selling a position. Fidelity employees continuously complained of Caspersen's "brinksmanship" in refusing to sell expiring options contracts up to the last minute before the contracts became worthless (*id.*). Fidelity's records highlighted the discrepancy between the $90,000 in Caspersen's account with the $50,000,000 in expiring options. Plaintiffs allege such activity constitutes "red flags for money laundering" (*id.*, ¶ 90).

Under FINRA rules dealing with money laundering, Fidelity was required to survey accounts to detect suspicious activity, and to monitor the flow of money to and from accounts. If Fidelity had taken these steps, plaintiffs allege, it would have seen and, upon information and belief, did see the dramatic changes in Caspersen's wire activity, as the amounts deposited went from $725,000 to $17 million from August 2014 through November 2015. Fidelity's records showed the address for each shell entity matched Caspersen's home address. Fidelity knew that Caspersen had wired tens of millions of dollars into his margin account from bank accounts maintained in the names of the shell entities, that he commingled the funds received from the shell entities in his personal margin account, that he converted the funds received from the different shell entities, that he wired out to his personal bank accounts approximately $10 million more than he had advanced to his Fidelity margin account from his personal bank accounts, and that the shell entities wired approximately $38 million more to Caspersen's margin account than the shell entities received back from the margin account.

In 2012, Caspersen opened a trading account at Interactive with $2 million. Under FINRA, Caspersen was obligated to inform Interactive that he was a FINRA registered broker who was employed by a broker. Interactive was obligated to obtain the employer's consent to the opening of Caspersen's account and send the employer duplicates of Caspersen's trading records. Interactive was required to use reasonable diligence to determine that the purchases and sales of securities did not adversely affect Caspersen's employer. Interactive did none of this.

In January 2013, Interactive investigated a potential money laundering concern relating to the account. Interactive learned Caspersen failed to disclose that he worked for a broker. Caspersen stopped trading at Interactive around February 2013, after he lost the $2 million. "Upon information and belief," when Caspersen later opened his other Interactive account in December 2015 and transferred the shell entities' money from Fidelity to Interactive, he did not identify his employer or indicate that he was a licensed broker employed by a licensed broker. Interactive learned in December 2015 that Caspersen was employed by a broker, but failed to inform his employer that Caspersen had opened the account and to obtain its consent. When Interactive learned Caspersen had not informed Interactive he worked for a broker, Interactive should have refused to open the account. If Interactive had done this, or subsequently informed Caspersen's employer about his account, it would have discovered the source of his funds and his reason for hiding his personal trading accounts from his employer.

Caspersen placed each trade by phoning an Interactive broker. Caspersen behaved irrationally and compulsively by weekly betting nearly the entire account. His account necessarily experienced massive swings in equity depending on the market's direction (complaint, ¶ 145). Within a couple of days of opening the 2015 account at Interactive, he started to have swings of $8 to $9 million a day in the equity value of his account. Under FINRA rules, this "sudden extensive wire activity," his recurrent deceit in opening accounts, and his unusual volume of trading activity should have prompted Interactive to survey his activity with "enhanced due diligence" (*id.*, ¶ 146). Interactive did nothing to stop his fraud until law enforcement became involved.

In determining a CPLR 3211 (a) (7) motion, the test is whether the challenged cause of action has been sufficiently stated within the four corners of the pleading (*see Frank v DaimlerChrysler Corp.*, 292 AD2d 118, 120-121 [1st Dept 2002]). The court accepts as true the facts alleged in the complaint as well as all reasonable inferences that may be gleaned from those

facts (*see Amaro v Gani Realty Corp.,* 60 AD3d 491, 492 [1st Dept 2009]; *McGill v Parker,* 179 AD2d 98, 105 [1st Dept 1992]). The court is not permitted "to assess the merits of the complaint or any of its factual allegations, but only to determine if, assuming the truth of the facts alleged, the complaint states the elements of a legally cognizable cause of action" (*P.T. Bank Cent. Asia v ABN AMRO Bank N.V.*, 301 AD2d 373, 376 [1st Dept 2003]). However, factual allegations that consist of legal conclusions or that do not state a viable cause of action are not accorded such consideration (*see Caniglia v Chicago Tribune-N.Y. News Syndicate,* 204 AD2d 233, 233-234 [1st Dept 1994]).

The first cause of action is for breach of contract against the shell entities. The second through sixth are against Fidelity, based on, respectively, DCL §§ 273, 274, 275, 276, and 276-a. The seventh and last cause of action is against Interactive, based on DCL §§ 273-278.

To state a cause of action for constructive fraudulent conveyance under DCL §§ 273, 274, and 275, the complaint must allege the transferor transferred assets without receiving fair consideration in exchange (*see ABN AMRO Bank, N. V. v MBIA Inc.*, 17 NY3d 208, 228 [2011]; *Carlyle, LLC v Quik Park 1633 Garage LLC*, 160 AD3d 476, 477 [1st Dept 2018]). A person can be liable for constructive fraud without any actual intent to defraud (DCL §§ 273, 274; 30 NY Jur 2d Creditors' Rights § 367).

Fair consideration must be given "in good faith" (DCL § 272). Good faith and fair consideration are intertwined and a transaction will be deemed to lack fair consideration if it was not made in good faith (*see American Panel Tec v Hyrise, Inc.*, 31 AD3d 586, 587 [2d Dept 2006]; *Matter of Mega Personal Lines, Inc. v Halton*, 9 AD3d 553, 555 [3d Dept 2004]). A plaintiff seeking to set aside a conveyance due to a lack of good faith must prove a lack of honest belief in the propriety of the transfer in question, an intent to take unconscionable advantage of others, or an intent to, or knowledge of the fact that the activities in question will, hinder, delay, or defraud a creditor of the transferor (*see Southern Indus. v Jeremias,* 66 AD2d 178, 183 [2d Dept 1978]; *see Sardis v Frankel*, 113 AD3d 135, 143 [1st Dept 2014]).

Fair consideration is "a fair equivalent" to the transferred property or an "amount not disproportionately small as compared with the value of the property" (DCL § 272 [a];*see Rubin v Manufacturers Hanover Trust Co.,* 661 F2d 979, 993 [2d Cir 1981]; *In re 375 Park Avenue Assocs., Inc.,* 182 BR 690, 695-96 [Bankr SD NY 1995]). Where the transferee gives equivalent value in exchange for the transfer, good faith is satisfied if the transferee acted without actual or

constructive knowledge of any fraudulent scheme (*see HBE Leasing Corp. v Frank*, 48 F3d 623, 636 [2d Cir 1995]; *Mendelsohn v Kovalchuk (In re APCO Merch. Servs.),* 585 BR 306, 317 [Bankr ED NY 2018]).

The Brokers argue the complaint does not adequately allege their failure to give fair consideration. The complaint does not allege the Brokers took commissions for unearned services, or that the commissions were extravagant or in any way unfair. The complaint alleges the Brokers did not transfer fair equivalent value in good faith to the shell entities in exchange for any of the transfers, because any consideration was given to Caspersen instead of to the shell entities, and the brokers had actual or constructive knowledge of Caspersen's fraudulent scheme.

The complaint fails to allege the Brokers were aware or should have been aware Caspersen was trading with other people's money or money taken under false pretenses. The complaint alleges the Brokers were aware Caspersen was and had been acting recklessly, but not fraudulently. The brokerage accounts were in Caspersen's name. That Caspersen transferred money held in the shell entities' names to an account in his own name or that the shell entities' addresses were the same as his does not suggest he was practicing deceit on third parties. Those facts do not indicate Caspersen had stolen money.

Plaintiffs contend the Brokers were on inquiry notice of Caspersen's fraud. Inquiry notice exists where the transferee has knowledge of facts that should reasonably put it on notice the transfer had a fraudulent purpose or the transferor was insolvent, pursuant to DCL § 272 (*see Christian Bros. High Sch. Endowment v Bayou No Leverage Fund, LLC (In re Bayou Group, LLC)*, 439 BR 284, 310 [SD NY 2010]). The knowledge must be specific to the transfer at issue (*id.* at 311). A transferee may be put on inquiry notice where the transferor promises unreasonable returns, has checks to investors returned for insufficient funds, the transfer is grossly in excess of the value the transferee provides, the transferor is suffering huge losses and simultaneously reporting 20% profit to investors (*see Christian Bros.,* 439 BR at 322 [SD NY 2010]; *In Bear, Stearns Sec. Corp. v Gredd (In re Manhattan Inv. Fund Ltd.),* 397 BR 1, 23-24 [SD NY 2007]). In this case, there is no indication that the Brokers had knowledge that should have indicated the possibility that the shell entities or Caspersen were insolvent or their money was not Caspersen's or he was using money that was not his. Caspersen transferring money from the shell entities does not mean he was taking money illegally. The transfer to Interactive

was made from the Fidelity account in Caspersen's name. The complaint does not allege Interactive knew about the existence of the shell entities.

Plaintiffs state Caspersen engineered a Ponzi scheme and urge the court to apply the Ponzi scheme presumption. A Ponzi scheme is "a pyramid scheme where earlier investors are paid from the investments of more recent investors, rather than from any underlying business concern, until the scheme ceases to attract new investors and the pyramid collapses" (*Eberhard v Marcu,* 530 F3d 122, 132 n 7 [2d Cir 2008]). The appellation Ponzi scheme applies "to any sort of inherently fraudulent arrangement under which the debtor-transferor must utilize after-acquired investment funds to pay off previous investors in order to forestall disclosure of the fraud" (*Bear, Stearns,* 397 BR at 12]). The Ponzi scheme presumption is that the scheme demonstrates actual intent to defraud as a matter of law (*id*. at 11).

At his plea allocution, Caspersen swore that, as to count one against him, he defrauded numerous people out of $38 million by falsely telling them he had an investment opportunity, but that, in reality, he just wanted to get money to gamble with. As to count two, he swore he defrauded his employer out of $8 million and eventually paid back the money with money obtained from the fraud described in count one. Even if count two could be described as a Ponzi scheme, it did not involve plaintiffs. Count one was not a Ponzi scheme. Plaintiffs allege the shell entities did not make any of the subsequently due interest payments after Caspersen was arrested in March 2016. However, plaintiffs do not allege Caspersen paid them money obtained from later investors. They do not allege Caspersen paid them or the shell entities any money before he was arrested.

As to Caspersen, rather than the shell entities, receiving consideration from the brokers, the complaint indicates the shell entities' monies at BOA, Fidelity, and Interactive were entirely controlled by Caspersen. The consideration given to Caspersen benefitted the shell entities, assuming they were the transferors. The transferor is regarded as receiving fair consideration if it indirectly receives value from the transaction (*see Rubin v Manufacturers Hanover Trust Co.,* 661 F2d 979, 991-92 [2d Cir 1981]; *Silverman v Actrade Capital, Inc. (In re Actrade Fin. Techs., Ltd.)*, 337 BR 791, 804 [SD NY 2005]).

Under DCL § 276, every conveyance made with actual intent to hinder, delay or defraud present or future creditors is fraudulent. Even where the transferee gives fair consideration, a transfer may be fraudulent if it was made with actual intent to hinder, delay or defraud a creditor

(*see Lippe v Bairnco Corp.,* 249 F Supp 2d 357, 374 [SD NY 2003], *affd* 99 Fed Appx 274 [2d Cir 2004]; *HBE,* 48 F3d at 633-6345]).

Interactive argues that the claim of actual fraud is deficient because plaintiffs do not allege that Caspersen had fraudulent intent, only that he had the intent to gamble to feed his addiction. However, the intent to gamble with other's money without their consent is fraudulent intent. Fraudulent intent may be inferred from the pleading, and Caspersen's fraudulent intent is inferable from the allegations that he took money under false pretenses (*see Marine Midland Bank v Zurich Ins. Co.,* 263 AD2d 382 [1st Dept 1999]). A guilty plea by a transferor of property is evidence of fraudulent intent (*see Matter of Wimbledon Fin. Master Fund, Ltd. v Bergstein,* 166 AD3d 496, 497 [1st Dept 2018]; *see McHale v Boulder Capital LLC (In re 1031 Tax Group, LLC)*, 439 BR 47, 72 [Bankr SD NY 2010]).

The brokers argue the claim for actual fraud should be dismissed because the complaint fails to plead that they, as well as Caspersen, had fraudulent intent. Federal cases have noted that New York law is not clear regarding whether it is the intent of the transferor or the transferee that is relevant for intentional fraud (*see Picard v Cohmad Sec. Corp. (In re Bernard L. Madoff Inv. Sec. LLC),* 454 BR 317, 331 [SD NY 2011]; *Picard v Estate of Chais (In re Bernard L. Madoff Inv. Sec. LLC),* 445 BR 206, 221 [SD NY 2011]; *Silverman,* 337 BR at 808). The soundest conclusion arrived at is that, on a motion to dismiss, only the intent of the transferor is relevant, and that the intent of the transferee must be raised as an affirmative defense on summary judgment or at trial (*see Picard,* 454 BR at 331; *Gowan v Patriot Group, LLC (In re Dreier LLP)*, 452 BR 391, 433-435 [SD NY 2011]). On a summary judgment motion in this court, the plaintiff must make a prima facie showing the transferor acted with fraudulent intent; then the burden shifts to the transferee to establish that it received the property for fair consideration and in good faith without knowledge of the fraud (*see Eastern Consol. Props., Inc. v Lynbrook Sunrise Realty LLC,* 2016 NY Slip Op 30711[U], *4 [Sup Ct, NY County 2016]; *Amalgamated Bank v Schneider & Schneider, Inc.,* 2016 NY Slip Op 30327[U] [Sup Ct, NY County 2016]; *Square Mile Structured Debt (ONE) LLC v Swig,* 2013 NY Slip Op 33064[U] [Sup Ct, NY County 2013]).

In spite of the foregoing, however, the court must evaluate motions to dismiss for failure to state a cause of action according to the usual standard. The complaint must point to some possibility of fraud on the part of the transferee and this complaint does not. The complaint fails to allege that the brokers did not give fair consideration or have good faith.

To recover under § 276, the plaintiff must show the transferee participated or acquiesced in the transferor's fraudulent act (*see DoubleLine Capital LP v Odebrecht Fin., Ltd.,* 323 F Supp 3d 393, 467 [SD NY 2018]; *Official Comm. of Unsecured Creditors of Vivaro Corp. v Leucadia Natl. Corp. (In re Vivaro Corp.),* 524 BR 536, 559 [Bankr SD NY 2015]; *Sullivan v Kodsi*, 373 F Supp 2d 302, 309 [SD NY 2005]). Under the DCL, a transfer made with fraudulent intent cannot be recovered against a transferee who takes for fair consideration and without knowledge (see *Balaber-Strauss v Sixty-Five Brokers (In re Churchill Mtge. Inv. Corp.),* 256 BR 664, 676 [Bankr SD NY 2000], *affd* 264 BR 303 [SD NY 2001]; *Securities Inv. Prot. Corp. v Rossi (In re Cambridge Capital, LLC),* 331 BR 47, 64 [ED NY 2005]; *HBE Leasing,* 48 F3d at 636). "Mutual fraudulent intention on the part of the parties to a transaction is required in order to invoke the protection of the law prohibiting fraudulent conveyances; fraudulent intent on the part of one of the parties is insufficient" (30 NY Jur 2d, Creditors' Rights § 354; 13 Carmody-Wait 2d § 85:34). Since the complaint fails to allege the transferees lacked fair consideration, good faith, and fraudulent intent, the claims for constructive and actual fraud must be dismissed.

DCL § 276-a provides that where a § 276 conveyance is found to have been made and received by the transferee with actual fraudulent intent, the creditor shall be awarded attorney's fees. DCL § 278 provides that a creditor whose claim has matured may set aside a fraudulent transfer "against any person except a purchaser for fair consideration without knowledge of the fraud . . . ." DCL §§ and 273-a and 277, concern, respectively, a transferor who makes a conveyance while a defendant in an action and a conveyance of partnership property, and do not pertain to this case. None of these claims apply.

It is hereby

ORDERED that motion sequence number 001 by defendant Fidelity Brokerage Services, LLC and motion sequence number 002 by defendant Interactive Brokers, LLC to dismiss the complaint are granted; and the complaint is hereby dismissed as to those defendants, with costs and disbursements to said defendants as taxed by the Clerk of the Court upon proper bills of

costs and the Clerk is directed to enter judgment accordingly in favor of said defendants; and it is further

ORDERED that the action is severed and continued against the remaining defendants.

This constitutes the decision and order of the court.

DATED: May 19, 2020 **E N T E R,**

O.P. Sherwood

O. PETER SHERWOOD J.S.C.