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

PRESENT: James A. Yates Justice PART 49

BALANCED RETURN FUND LIMITED, MENDOTA CAPITAL, INC., COMMAX INVESTORS SERVICES LTD., and COMPREHENSIVE INVESTORS SERVICES, LTD., - v -

ROYAL BANK OF CANADA, RBC CAPITAL SERVICES, et seq.

INDEX NO. ~~600949-09~~
MOTION DATE
MOTION SEQ. NO. 002
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

is decided in accordance with the attached Decision and Order, dated February 17, 2010.

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

Dated: 2-17-10

FEB 23 2010

J.S.C.

Check one: FINAL DISPOSITION X NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST

James A. Yates

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

BALANCED RETURN FUND LIMITED; MENDOTA CAPITAL, INC., COMMAX INVESTORS SERVICES LTD.; and COMPREHENSIVE INVESTORS SERVICES, LTD.,	
Plaintiffs,	
-against-	Decision and Order Index No. 600949-2009
ROYAL BANK OF CANADA; RBC CAPITAL SERVICES, INC.; RBC ALTERNATIVE ASSETS L.P., successor to RBC; RBC CAPITAL MARKETS CORP. formerly known as RBC DOMINION SECURITIES,	
Defendants.	

Hon. James A. Yates, J.S.C.

On June 17, 2009, defendants moved to dismiss plaintiffs' complaint pursuant to CPLR §§ 3211 (a) (1) (defense founded on documentary evidence), (5) (defense founded on statute of limitations grounds) and (7) (failure to state a cause of action). Defendants' first sought dismissal of the complaint on forum non conveniens and statute of limitations grounds. That part of defendants' motion to dismiss was denied by the Court on November 18, 2009.

The plaintiffs in this action are Balanced Return Fund Limited, Mendota Capital, Inc., Commax Investors Services Ltd. and Comprehensive Investors Services. For the reasons that follow, the motion to dismiss the complaint is denied.

Background

On March 27, 2009, plaintiffs, a group of investors in Olympus United Funds (Olympus) and two other subsidiary funds, filed a lawsuit against Royal Bank of Canada (RBC) and two bank securities units over the 2005 collapse of the funds offered by defunct Norshield Financial Group (Norshield). Plaintiffs allege that they lost approximately $90 million as a result of the funds' collapse. Specifically, plaintiffs allege that Olympus United Funds was fronted by Norshield, but secretly managed by Royal Bank of Canada through its New York subsidiary.

Plaintiffs assert that Norshield was RBC's broker - dealer affiliate. Plaintiffs further allege that in dealing with Norshield, RBC assumed discretionary control of their investments and exercised control in key areas, including financial reports and prospectuses. Defendants allegedly overstated their funds' assets, breached their fiduciary duties to investors, and committed a massive fraud by misrepresenting material facts, including the nature of the investment, the investment risks and assets held by Olympus. Plaintiffs allege that RBC earned over $60 million from the fund.

The complaint also alleges that RBC appointed Royal Bank of Canada Capital Markets Corporation (RBCCMC) to act on its behalf as agent. Royal Bank of Canada Capital Services (RBC Services) was an indirect wholly owned subsidiary of RBC whose sole purpose was to provide various services to and for the benefit of RBC, including negotiating and entering into investment management agreements with certain portfolio managers who managed fund assets. RBC Services, on behalf of RBC, was signatory to the agreement with each hedge fund manager it retained.

The complaint seeks damages for breach of fiduciary duty, aiding and abetting breach of fiduciary duty, fraud, unjust enrichment and restitution, and breach of contract as third party beneficiaries of the contracts between RBC and Norshield.

Discussion

Standard of Review

A complaint should be dismissed if it fails to state a cause of action (*see* CPLR § 3211 (a) [7]). In evaluating the adequacy of a complaint, the Court is required to read the complaint generously, accept the truth of the allegations and draw all reasonable inferences from the allegations (*see EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005]; *Sokoloff v Harriman Estates Dev. Corp.*, 96 NY2d 409, 414 [2001]; *Leon v Martinez*, 84 NY2d 83 [2003]). A dismissal of the complaint is warranted under CPLR § 3211 (a) (1) only if the documentary evidence submitted to the Court conclusively establishes a defense to the asserted claims as a matter of law (*see Hopkinson v Redwing Constr. Co.*, 301 AD2d 837, 837-838 [3d Dept 2003]). The complaint should provide "plausible grounds" for the allegations with "enough facts to raise a reasonable expectation that discovery will reveal evidence" to support them (*Bell Atlantic Corp. v Twombly*, 550 US 544 [2007]). Finally, the inquiry on a motion to dismiss is not whether plaintiffs will ultimately prevail, but whether plaintiffs are entitled to offer evidence to support their claims.

Count I: Breach of Fiduciary Duty

In asserting a claim for breach of fiduciary duty, plaintiffs must prove the existence of a fiduciary relationship. A fiduciary relationship is characterized by an unusual degree of trust and confidence between parties, one of whom has superior knowledge or skill and is under a duty to represent the interests of the other (*see e.g. Flickinger v Harold C. Brown & Co.*, 947 F2d 595, 600 [2d Cir 1991]). Defendants contend that they owed no duty to plaintiffs. Defendants further argue that unless RBC was plaintiffs' agent in a conventional sense, they did not serve as fiduciaries.

New York courts have recognized that not all business relationships implicate a fiduciary relationship or duty. At the same time, however, the courts have refused to define a fiduciary duty in precise detail and in a manner that would exclude new factual situations. Such a relationship is a fact-specific inquiry (*EBC I, Inc. v Goldman, Sachs & Co.*, 5 NY3d 11, 19 [2005] [Court of Appeals found complaint stated a breach of fiduciary duty claim where plaintiff alleged relationship of the parties went beyond arm's length to one of higher trust and confidence]).

An independent contractor such as a bank, attorney, or even a broker conducts an independent business. That fact does not mean that he may not come under a duty to disclose material facts when he assumes a relationship of trust and confidence to another. In that case, the relationship becomes one of agency. (Restatement [Second] of Agency, § 14N, at 80 [1958]). The duty to disclose material facts imposed on '[o]ne who in course of his business or profession supplies information for the guidance of others in their business transactions (Restatement of Torts, § 552 [1938]) includes the duty to disclose information which in the exercise of due care he should know." *Id.* at § 552, Comments c, d, e. As stated in Comment d:

> "Where the information concerns a fact not known to the recipient, he is entitled to know that the supplier will exercise that care and competence ins its ascertainment which the supplier's business or profession requires and which,therefore, the supplier professes to have by engaging in it. Thus, the recipient is entitled to expect such investments as are necessary will be carefully made and that his informant will have normal business or professional business competence to form an intelligent judgment upon the data

obtained thereby."

And in Comment e:

"If the matter is one which requires investigation,

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the supplier of the information must exercise reasonable care and competence to ascertain the facts on which his statement is based . . .He must exercise reasonable care and competence in communicating the information so that it may be understood by the recipient."

The allegations in plaintiffs' complaint give rise to permissible inferences which are sufficient to sustain this cause of action. Plaintiffs allege that defendants were responsible for the investment decisions in plaintiffs' portfolios managed by defendants. They exercised discretionary control over the investments in the Fund. RBC Capital and RBC Services, on behalf of RBC, had veto and termination power over the portfolio advisors and RBC Services conducted due diligence on these advisors *(see Bissel v Merrill Lynch & Co.*, 937 F Supp 237, 246 [SD NY 1996]). They assert that defendants violated their duty of care by negligently failing to manage the assets of their investment accounts, failing to pursue a prudent investment strategy and by failing to eliminate conflicts of interest.

Defendants' submissions do not conclusively disprove plaintiffs' theory or negate the factual allegations that RBC concealed its role as actual manager of the Fund. Without formal discovery, plaintiffs cannot test RBC's argument that it had no investment management responsibilities with respect to plaintiffs' monies. After the benefit of discovery and on a motion for summary judgment, the Court may be better able to determine whether RBC had no fiduciary duty to plaintiffs because its role was ministerial or administrative only (*see Jordan (Bermuda) Inv. Co. v Hunter Green Invs. LLC*, 2007 WL 2948115, 2007 US Dist LEXIS 75376 [SD NY Oct. 3, 2007]) ("Where, as here, '[t]here is no competent evidence that [defendant] participated in any investment of [plaintiff's] funds,' and instead merely provided nondiscretionary administrative services, no fiduciary duty exists.") (citation omitted).

As well, plaintiffs' allegations are sufficient to plead proximate cause under prevailing law. Thus, plaintiffs' first cause of action for breach of fiduciary duty is pled adequately.

Count II: Aiding and Abetting a Breach of Fiduciary Duty

To plead a prima facie case for aiding and abetting a breach of fiduciary duty, plaintiffs must allege that defendants substantially assisted the primary violator *(see King v George Schonberg & Co.*, 233 AD2d 242, 243 [1st Dept 1996] ["In the absence of a confidential or fiduciary relationship between plaintiff and her brother's attorneys giving rise to a duty of disclosure, the silence of the attorneys did not amount to the substantial assistance that is a required element of aider and abetter liability."]). Allegations of mere inaction are insufficient to sustain the claim unless the defendant has an independent duty to plaintiff (*King, supra; Superintendent of Ins. of State of NY v Spira*, 289 AD2d 173 [1st Dept 2001]).

In the second claim for aiding and abetting a breach of fiduciary duty, plaintiffs incorporate the allegations of the first count and further allege that each of the defendants knew of the numerous breaches of fiduciary duty by the Norshield Financial Group and aided and abetted in the commission of wrongful acts. As well, plaintiffs argue that each of the defendants participated in the misconduct, and aided and ratified the alleged misconduct for its own benefit, resulting in a huge loss of funds to plaintiffs. Specifically, plaintiffs allege that the RBC defendants "knew, understood, and helped develop the structure of [the Fund]; conducted due diligence related to the Fund; and approved certain transactions designed to mask the Fund's financial problems." (*See* Compl.¶ 6; Compl. ¶ 3, 23-24, 26, 29, 41-42, 44, 46; *see also Yuko Ito v Suzuki*, 57 AD3d 205 [1st Dept 2008] [holding plaintiff had sufficient pled aiding and abetting claim where she alleged defendants had helped structure transactions with fiduciary to the detriment of plaintiff]). Accordingly, the Court finds that sufficient facts have been alleged to sustain this cause of action for now.

Count III: Fraud

The third claim for fraud clearly demonstrates fraud by concealment. The complaint alleges that RBC and Norshield Financial Group began doing business together as early as 1999, and that RBC was involved in the creation, marketing and management of assets in "funds of funds" alternative investments. Nonetheless, it is claimed that defendants concealed RBC's role, interests and actions. RBC also allegedly provided leveraged financial investments offered by investors by Norshield and its successors whose terms were skewed to favor RBC's control and operation of the funds' investments. Furthermore, plaintiffs allege that RBC knew that the Fund overstated its net asset values, concealed its highly leveraged structure and illiquidity of many of its assets in the Fund's informational materials, and knew the Fund allowed favored

investors (not plaintiffs) to redeem fund shares at inflated values to the detriment of other investors. The complaint also alleges that the RBC defendants participated in a plan or course of conduct that was fraudulent; knew or should have known that their representations to plaintiffs were false; and made those representations intentionally. Defendants participated and substantially assisted in an alleged fraud perpetuated by RBC. They solicited monies from defendants and other investors with promises of high returns. Plaintiffs were misled by Norshield on how their $500 million was being invested but did not disclose these misrepresentations to plaintiffs. As the fraud became public and began to fall apart, RBC refused plaintiffs' requests to have their monies returned to them. The allegations are pleaded with particularity and adequately state a cause of action for fraud.

Count V: Unjust Enrichment

Under New York law, an unjust enrichment claim is sufficiently alleged when the complaint alleges "(1) that the defendant was enriched; (2) that the enrichment was at the plaintiff's expense; and (3) that the circumstances are such that in equity and good conscience the defendant should return the money or [benefit] to the plaintiff." (*Bazak Intern Corp. v Tarrant Apparel Group*, 347 F Supp2d*1, *3-4 [SD NY 2003] quoting *Golden Pacific Bancorp v Federal Deposit Ins. Corp.*, 273 F3d 509, 519 [2d Cir 2001]).

Here, plaintiffs allege that defendants received fees in excess of $60 million dollars in connection with the management and trading of investments in the Fund. More importantly, plaintiffs allege that defendants did not properly earn or were entitled to this benefit. Additionally, plaintiffs allege that at the expense of investors, defendants improperly retained the proceeds of the underlying securities after they terminated an option. Accordingly, plaintiffs will be allowed the benefit of discovery.

Count VI: Breach of Contract as Third-Party Beneficiaries

Under the test outlined in the Restatement (Second) of Contracts and followed by New York courts, a party claiming third-party beneficiary status must allege: "(1) the existence of a valid and binding contract between the other parties; (2) that the contract was intended for his primary benefit; and (3) that the benefit to him is sufficiently immediate, rather than incidental, to indicate the assumption by the contracting parties of a duty to compensate him if the benefit is lost." (*State of Cal. Pub. Employees' Ret. Sys. v Sherman & Sterling*, 95 NY2d 427[2000]; *see also Levin v Tiber Holding Corp*, 277 F3d 243, 248 [2d Cir 2002]

[internal citation omitted]; *Fourth Ocean Putnam Corp. v Interstate Wrecking Co.*, 66 NY2d 38, 43-44 [1985]). If plaintiffs are able to establish these elements, than they may have enforceable rights under the contract in question. (*Flickinger v Harold C. Brown & Co.*, 947 F2d 595, 600 [2d Cir 1991] [finding that a person is an "intended beneficiary" of a contract "if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either (a) the performance of the promise will satisfy an obligation to pay money to the beneficiary; or (b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance."].)

Accepting the facts as alleged in the complaint as true and according plaintiffs the benefit of every possible favorable inference, the Court finds Here, plaintiffs have adequately alleged that they were the intended third party beneficiaries of the contract between Norshield and RBC. Because the facts fit into a cognizable legal theory, plaintiffs will be permitted to proceed on this claim.

Although it is unclear at this time whether plaintiffs will ultimately succeed in establishing their claims, the Court finds that plaintiffs have asserted cognizable causes of actions for all their claims against defendants and therefore, defendants' motion to dismiss the complaint is denied.

Accordingly, it is

ORDERED that the motion to dismiss is denied.

This constitutes the Decision and Order of the Court.

Dated: February 17, 2010

ENTER:

James A. Yates, J.S.C.

James A. Yates

FEB 23 2010