UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

BANK OF AMERICA, NATIONAL ASSOCIATION, BANC OF AMERICA SECURITIES LLC, and U.S. BANK NATIONAL ASSOCIATION, solely in its capacity as Trustee under the Indenture	:	
Plaintiffs, and	:	Civil Action No. 08cv9265 (AJN)
BANC OF AMERICA SECURITIES LLC,	:	ECF Case
Counter Defendant,	:	
- against -	:	
BEAR STEARNS ASSET MANAGEMENT INC., RALPH CIOFFI, MATTHEW TANNIN, and RAYMOND McGARRIGAL,	:	
Defendants/Counter Claimants	:	

COUNTER DEFENDANT BANC OF AMERICA SECURITIES LLC'S MEMORANDUM OF LAW IN SUPPORT OF ITS MOTION FOR SUMMARY JUDGMENT ON COUNTER CLAIMANTS' COUNTERCLAIMS

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Counter Defendant Banc of America Securities LLC ("BAS") submits this memorandum in support of its motion for summary judgment on counter claimants' Counterclaims, which seek contribution from BAS for allegedly aiding and abetting BSAM's breach of fiduciary duties. As we show below, the Counterclaims are squarely foreclosed by Second Circuit precedent.

PRELIMINARY STATEMENT

The Counterclaims come into play only if defendants have been found liable for breach of fiduciary duty. *See, e.g.*, BSAM Counterclaim (Doc. 100) ¶ 7. Accordingly, the jury would not consider these claims unless it has already found that: 1) as Collateral Manager responsible for the selection of the CDO^2's collateral, BSAM had a fiduciary duty to the Issuer; 2) BSAM breached that duty by causing the Issuer to purchase overvalued collateral (the "Initial Collateral") from its own struggling Funds; and 3) BSAM's breach proximately caused the Issuer's damages when those assets plunged in value after the market learned about the dire state of the Funds.

If the jury so finds, defendants hope to get some help in paying the damages they inflicted on their own beneficiary. Their preferred candidate? BAS, which had *no* fiduciary duties to the Issuer and knew *nothing* about the Funds' problems until hours before the closing of the transaction. And what did BAS do to become an alleged aider-and-abettor? It proceeded with a previously agreed-upon transaction in an attempt to protect its shareholders—to whom it *did* owe duties—from the consequences of BSAM's fraud and breach of contract.[1] Defendants' Counterclaims presuppose that BAS was obligated to sacrifice its *own* interests (and those of its shareholders) in order to protect the *Issuer* from a disloyal, self-dealing fiduciary.

[1] See Plaintiffs' Memorandum in Opposition to Defendants' Motion for Summary Judgment ("S.J. Opp.") at 3–10.

The law imposes no such obligation. To the contrary, dispositive Second Circuit precedent entitled BAS to transfer the Initial Collateral to the Issuer, exactly as it did. *See Sharp Int'l Corp. v. State Street Bank & Trust Co. (In re Sharp Int'l Corp.)*, 403 F.3d 43, 51 (2d Cir. 2005) (rejecting an aiding-and-abetting a breach of fiduciary duty claim where "the complaint sa[id] no more than that [defendant] relied on its own wits and resources to extricate itself from peril, without warning persons it had no duty to warn.")

BACKGROUND

The material facts are few and undisputed:[2] The CDO^2 transaction was scheduled to close on May 24, at which time the Issuer would purchase the Initial Collateral, obtained entirely from BSAM's two flagship funds. BAS agreed to facilitate the closing by purchasing the Initial Collateral from the Funds on May 22 and transferring it to the Issuer (at the same prices) two days later. Counter Defendant BAS's Rule 56.1 Statement ("Stmt.") ¶¶ 3–5. Accordingly, on May 22, BAS paid the Funds $2.86 billion for the Initial Collateral that BSAM had earmarked for transfer to the Issuer. *Id.* ¶ 5. The next day, on May 23, BAS put that Initial Collateral into an escrow account at the Issuer's trustee, LaSalle Bank N.A. ("LaSalle"), pending the closing of the deal. At closing, LaSalle was to release the Initial Collateral to the Issuer. *Id.* ¶¶ 6–7. That evening, BAS received BSAM's May 23 Letter about redemption levels in the EL Fund. *Id.* ¶ 8. Had BofA decided to pull out of the deal at that point, LaSalle would have returned the Initial Collateral to BAS instead of releasing it to the Issuer as planned. *Id.* ¶ 7. In other words, BofA would have paid the Funds $2.86 billion for outright ownership of the Initial Collateral.

In an attempt to mitigate its risk and protect its shareholders, BofA decided to proceed with the CDO^2 closing. *Id.* ¶¶ 9–10. The Initial Collateral accordingly transferred from

[2] For a full recitation of the factual background of the CDO^2 transaction, see S.J. Opp. at 3–13.

escrow to the Issuer—just as BSAM had designed and in accordance with BAS's pre-set release instructions. *Id.* ¶¶ 3, 11. By proceeding in this fashion, BAS avoided the direct risk of owning the Initial Collateral, while assuming the underwriting risk of having to purchase the Super Senior tranches of the CDO^2 if they were no longer marketable. BAS also obtained what it believed to be an added benefit: BSAM's purchase of the junior tranches of the CDO^2. Had BSAM fully honored this obligation—had it not instead transferred those tranches to another BofA department on repo[3]—BAS would have obtained extra layers of security, further mitigating the risk to which BSAM's misconduct had exposed the Bank. *Id.* ¶ 10. It is this decision to proceed to closing—rather than scuttling the prearranged deal and outright purchasing $2.86 billion in Initial Collateral—that defendants allege constitutes aiding and abetting. *See, e.g.*, BSAM Counterclaim (Doc. 100) ¶ 6.

ARGUMENT

Under New York law, one of the elements of aiding and abetting a breach of fiduciary duty is that the defendant "knowingly induced or participated in" the underlying breach.[4] *See Sharp*, 403 F.3d at 49 (quoting *Kaufman v. Cohen*, 760 N.Y.S.2d 157, 169 (1st Dep't 2003)). There is no colorable argument that BAS *induced* BSAM to violate its fiduciary duties; after all, BAS had no inkling of the breach until May 23, which was *after* BSAM had already sold the

[3] BAS's CDO bankers did not know about this repo transaction when they made the decision to close. Stmt. ¶ 10.

[4] Another element is that BAS had "actual knowledge" of BSAM's breach as of May 24. *Cf. Sharp*, 403 F.3d at 50 (assuming, without deciding, the sufficiency of "actual knowledge" allegations). We dispute that element as well. As of May 24, BAS did not know all of the information that BSAM had concealed: that redemptions plagued the HG Fund, that liquidation planning was underway for both Funds, and that BSAM was trying to offload its entire high-grade platform (including its CDO-management business) onto a third-party "angel investor." *See* S.J. Opp. at 6–7. But we recognize that the Court will draw *all* possible inferences from the evidence in counter claimants' favor on BAS's motion for summary judgment on the Counterclaims. *See Gibson v. Am. Broad. Companies, Inc.*, 892 F.2d 1128, 1132 (2d Cir. 1989). We therefore assume, but do not concede, that a jury could find that the May 23 letter provided BAS with "actual knowledge" of BSAM's breach of its fiduciary duties to the Issuer.

overvalued Initial Collateral to BAS to facilitate its prearranged transfer to the Issuer. *See Sharp*, 403 F.3d at 51 (request by defendant "could not have 'induced'" a fraud that had already begun).

So defendants are left with "knowing participation" in BSAM's breach. But "knowing participation" requires "substantial assistance" and "[s]ubstantial assistance may only be found where the alleged aider and abettor 'affirmatively assists, helps conceal or fails to act *when required to do so*, thereby enabling the breach to occur.'" *Id.* (quoting *Kaufman*, 760 N.Y.S.2d at 157) (emphasis added). Conversely, as *Sharp* makes clear, "a company in a position to thwart or expose a breach of fiduciary duty may protect its interests by doing neither, sitting tight, and being quiet."[5] *Id.* at 52. And that is exactly what BAS did: it simply proceeded with a pre-arranged asset transfer to the Issuer in the hope that doing so would mitigate its losses due to defendants' misconduct. *See id.* at 51; *see also Chemtex, LLC v. St. Anthony Enters., Inc.*, 490 F. Supp. 2d 536, 548 (S.D.N.Y. 2007) (a non-fiduciary "has the right to protect its own interests . . . and such decisions cannot give rise to a claim that [the party] substantially assisted" another party's tort). Defendants are wrong, as a matter of law, that BAS was instead required to keep all the tainted assets on its books, and risk even greater losses.

Sharp is dispositive. There, controlling shareholders looted funds that their company had obtained from lenders on the basis of fraudulently inflated sales figures. 403 F.3d at 46–47. When one of those lenders uncovered the fraud, it quietly arranged for the company to repay its *own* loan from the proceeds of *new* loans; it did not blow the whistle and leave itself in harm's way. *Id.* at 47–48. Indeed, this lucky lender even provided consents that enabled the borrower to secure the new loans that bailed the lucky lender out. Over the next year, the controlling

[5] More might be expected of BAS if it, too, owed a fiduciary duty to the Issuer. But, as in *Sharp*, defendants "do[] not contend that [BAS] owed [the Issuer] a fiduciary duty." 403 F.3d at 51.

shareholders looted an additional $19 million from the company (including from the proceeds of the new loans). *Id.* at 48. When all the misconduct finally came to light, the company's bankruptcy trustee sued the repaid lender for having aided and abetted the controlling shareholders' breach of fiduciary duties to the company. *Id.* at 51–53.

The Second Circuit rejected that claim. It concluded that even if the lender had "actual knowledge" of the controlling shareholders' breach, it did not "knowingly participate" in it. The court explained that the lender's silence or inaction—in pursuit of its own self-interest—cannot sustain aiding-and-abetting liability. *See id.* at 52; *Kaufman*, 760 N.Y.S.2d at 170. The decision to proceed with a normal, self-interested business transaction simply cannot "constitute[] substantial assistance" of another party's breach of fiduciary duty. *Sharp*, 403 F.3d at 50–51; *see also Banco Industrial de Venezuela, C.A. v. CDW Direct, L.L.C.*, No. 11 Civ. 2082 (JGK), 2012 WL 3776367, at *6 (S.D.N.Y. Aug. 31, 2012) (plaintiff "offer[ed] no allegations that [the purported aider-and-abettor] was doing anything other than offering its normal services").

Nor does it matter, in the wake of *Sharp*, that BAS took affirmative action by closing the deal. Plaintiffs in *Sharp* alleged affirmative conduct as well—namely, that the lender actively participated in the looter's wrongdoing by providing its "contractually required consent" to allow the looted company to take on additional debt. 403 F.3d at 52. The Second Circuit acknowledged that the "grant of consent can be characterized as affirmative" because the lender had to "utter or write a consent without which Sharp could not have borrowed additional funds." *Id.* But the consent was "mere forbearance" and therefore did *not* constitute substantial assistance. *Id.*

So too here: the only "action" that can be attributed to BAS is its *forbearance* from derailing a previously agreed upon deal. Just as in *Sharp*, BAS merely "removed an

impediment" by agreeing to close, and this was a decision it was entitled to make "in its own interest." *Id.* And just as in *Sharp*, BAS's ability to sidetrack the deal "did not entail a duty to consider the interests of anyone else." *Id.* In short, BAS's "exercise of that right to protect itself . . . did not constitute participation" in BSAM's breach of fiduciary duty. *Id.*

Halo-Tech Hldgs., Inc. v. Cooper, No. 3:07 Civ. 489 (AHN), 2008 WL 877156, at *22 (D. Conn. Mar. 26, 2008), a case applying *Sharp* to nearly-identical Connecticut law, illustrates the same point. Because "continued participation in a transaction *cannot* constitute substantial assistance," (*id.* at *21 (emphasis added)), the court refused to require the defendant to "withdraw from the already-proposed transaction." *Id.* at *22. In the present case, the transaction was not merely "proposed"—it was hours away from closing—and BSAM itself had pre-arranged the ultimate transfer of the collateral to the Issuer. BSAM cannot now argue that BofA was required to pull out of the transaction and expose its own shareholders to additional risk in order to avoid being implicated in BSAM's self-dealing.

In sum, BAS engaged only in the "not . . . unusual activity" (*Kaufman*, 760 N.Y.S.2d at 170) of transferring the Initial Collateral to the Issuer in an industry-standard transaction. BAS did so in a rightful—indeed, obligatory—effort to mitigate its losses and "protect its own shareholders." *Sharp*, 403 F.3d at 52. Because such conduct cannot, as a matter of law, give rise to aiding-and-abetting liability, it provides no basis for defendants' Counterclaims for contribution.

CONCLUSION

For the foregoing reasons, BAS's motion for summary judgment on counter claimants' Counterclaims should be granted.

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Washington, D.C.

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