SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY

PRESENT: HON. EILEEN BRANSTEN J.S.C. *Justice* PART 3

Index Number : 600057/2006
RGH LIQUIDATING TRUST
vs.
DELOITTE & TOUCHE LLP
SEQUENCE NUMBER : 021
SUMMARY JUDGMENT

INDEX NO. 600057/2006
MOTION DATE 10/2/12
MOTION SEQ. NO. 021

The following papers, numbered 1 to 3, were read on this motion to/for summary judgment

Notice of Motion/Order to Show Cause — Affidavits — Exhibits	No(s). 1
Answering Affidavits — Exhibits	No(s). 2
Replying Affidavits	No(s). 3

Upon the foregoing papers, it is ordered that this motion is

IS DECIDED

IN ACCORDANCE WITH ACCOMPANYING MEMORANDUM DECISION

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

Dated: June 6, 2013 [signature], J.S.C.

1. CHECK ONE: ☑ CASE DISPOSED ☐ NON-FINAL DISPOSITION
2. CHECK AS APPROPRIATE: MOTION IS: ☑ GRANTED ☐ DENIED ☐ GRANTED IN PART ☐ OTHER
3. CHECK IF APPROPRIATE: ☐ SETTLE ORDER ☐ SUBMIT ORDER ☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART 3
---X
THE RGH LIQUIDATING TRUST, on behalf of:
RELIANCE GROUP HOLDINGS, INC.;
THE GENERAL UNSECURED CREDITORS
OF RELIANCE GROUP HOLDINGS, INC.;
RELIANCE FINANCIAL SERVICES CORP. (n/k/a
Reorganized RFS Corporation); and
THE GENERAL UNSECURED CREDITORS OF
RELIANCE FINANCIAL SERVICES CORP.,

Plaintiffs,

Index No. 600057/06
Motion Seq. No.: 021, 022 & 023
Motion Date: 10/2/12

-against-

DELOITTE & TOUCHE LLP and JAN A. LOMMELE,

Defendants.
---X

EILEEN BRANSTEN, J.:

Motion sequence numbers 021, 022, and 023 are consolidated for disposition.

This action is based upon Defendants' allegedly improper performance of actuarial and accounting services for Reliance Group Holdings, Inc. ("Reliance Group Holdings" or "RGH"), Reliance Financial Services Corp. ("Reliance Financial Services" or "RFS"), and Reliance Insurance Company ("RIC") (together, "Reliance"). Plaintiff RGH Liquidating Trust commenced this action, asserting fraud claims on behalf of the general unsecured creditors of RGH and RFS, including: a syndicate of 15 banks that collectively loaned RFS $237.5 million ("Banks");[1] the Pension Benefit Guaranty Corporation ("PBGC"); and two former employees of RGH and RFS, David Woodward ("Woodward") and Christine Howard ("Howard").

Background

RGH is a publicly held company that owned 100% of the stock of RFS, which, in turn, owned 100% of the stock of RIC. RIC generated more than 90% of the income of RGH, whose principal business was its ownership, through RFS, of RIC and its property and casualty insurance subsidiaries. Since 1996, defendant Deloitte & Touche LLP ("Deloitte") served as the independent outside accountant and auditor for RGH, RFS, and RIC, supplying annual audits of their financial statements. Defendant Jan A. Lommele ("Lommele"), as RIC's actuary, was responsible for assessing the adequacy of RIC's loss reserves.

Plaintiff's fraud claims are based upon financial reports prepared by Defendants for the year ending December 31, 1999, including Deloitte's audit and financial statements, issued on May 30, 2000, and Lommele's statement of actuarial opinion,

[1] According to the Amended Complaint, the Banks included Chemical Bank, Bank of America of Illinois, Bank of New York, Bankers Trust Company, Credit Lyonnais New York Branch, Credit Lyonnais Caymen Islands Branch, National Westminster Bank USA, Bank of Montreal, Corestates Bank, N.A., Union Bank, ABN AMRO Bank N.V., New York Branch, Sanwa Bank California, Banque Paribas, New York Branch, The Yasuda Trust and Banking Co., Ltd., and PNC Bank, National Association.

issued on February 25, 2000. Plaintiff claims that these financial reports overstated Reliance's surplus by $500 million and underreported its loss reserves by $500 million, resulting in a total misrepresentation of $1 billion. These misstatements allegedly caused Reliance to make improper distributions, incur additional liabilities, and forestall regulatory action.

It is undisputed that Reliance's financial condition was deteriorating by the end of 1999, prior to the issuance of Defendants' reports. RGH suffered an operating loss of $318.3 million in 1999, and, in February 2000, announced that it was suspending quarterly dividends and extending the maturity of its bank loans. In May 2000, RGH reported a $36.5 million operating loss for the first quarter of 2000. By June 2000, RIC stopped underwriting property and casualty insurance. In July, a deal for an outside company to acquire RGH collapsed, and various ratings agencies downgraded Reliance's rating. By December 2000, RGH's stock traded at less than $1.00 per share, and the New York Stock Exchange suspended trading of RGH's securities.

In June 2001, RGH and RFS filed for Chapter 11 bankruptcy protection in the United Statues Bankruptcy Court for the Southern District of New York. In October 2002, the Insurance Commissioner of the Commonwealth of Pennsylvania, as liquidator of RIC, commenced an action against Deloitte based upon the acts that are the subject of the instant action. By order dated November 7, 2005, the Bankruptcy Court named James

A. Goodman as Trustee of the RGH Liquidating Trust and authorized it to litigate the claims of RGH and RFS.

RGH Liquidating Trust commenced the instant action on January 6, 2006. The original complaint asserted claims for accounting and actuarial fraud, breach of contract, and fraudulent conveyance. Upon Defendants' motion to dismiss, the court dismissed the complaint, with leave to replead, in *RGH Liquidating Trust v. Deloitte & Touche LLP*, 13 Misc.3d 1219(A), 2006 NY Slip Op 51908(U) (Sup. Ct. N.Y. Cty. 2006), *affd* 47 A.D.3d 516 (1st Dep't 2008).[2]

In November 2007, Plaintiff filed an Amended Complaint, which is the operative pleading herein. The Amended Complaint asserts one cause of action for actuarial fraud and one cause of action for accounting and auditing fraud. Defendants moved to dismiss the amended pleading, which the court granted with respect to certain unidentified creditors but otherwise denied. *RGH Liquidating Trust*, 17 Misc.3d 1128(A), 2007 NY Slip Op 52181(U) (Sup. Ct. N.Y. Cty. 2007), *aff'd in part, modified in part* 71 A.D.3d 198 (1st Dep't 2009), *revd* 17 N.Y.3d 397 (2011).

Defendants now move for summary judgment, seeking dismissal of the Amended Complaint, as it remains, in its entirety. In particular, Defendants seek dismissal as to the

[2] Although the trial court dismissed the breach of contract cause of action as barred by judicial estoppel, the First Department held that this cause of action was "in essence a claim of professional malpractice," and affirmed dismissal of the breach of contract cause of action as a time-barred malpractice claim. *RGH Liquidating Trust*, 47 A.D.3d at 517.

claims of the Banks (motion sequence number 021), the PBGC (motion sequence number 022), and Woodward and Howard (motion sequence number 023). For the reasons that follow, Defendants' motions for summary judgment are granted.

Analysis

Defendants seek summary judgment dismissing the Amended Complaint, arguing that Plaintiff lacks standing and that the claims are barred by res judicata. On the merits, Defendants argue that Plaintiff's fraud claims should be dismissed for failure to establish proximate cause and reasonable reliance.

I. **Summary Judgment Standard**

It is well-understood that summary judgment is a drastic remedy and should be granted only if the moving party has sufficiently established the absence of any material issues of fact, requiring judgment as a matter of law. *Vega v. Restani Constr. Corp.*, 18 N.Y.3d 499, 503 (2012) (citing *Alvarez v. Prospect Hosp.*, 68 N.Y.2d 320, 324 (1986)). Despite the sufficiency of the opposing papers, "the failure to make such a showing requires denial of the motion." *Winegrad v. New York Univ. Med. Ctr*, 64 N.Y.2d 851, 853 (1985).

Once this showing has been made, the burden shifts to the party opposing the motion to produce evidentiary proof, in admissible form, sufficient to establish the existence of material issues of fact which require a trial of the action. *Zuckerman v City of New York*, 49 N.Y.2d 557, 562 (1980).

II. Procedural Issues

Defendants argue that Plaintiff lacks standing, because any injury is derivative. Defendants also argue that Plaintiff's claims are barred by res judicata, because Plaintiff failed to properly reserve the fraud claims in the bankruptcy proceedings. Defendants assert these threshold procedural arguments as grounds for dismissing the Amended Complaint in its entirety.

A. *Derivative Standing*

Defendants argue that the Banks lack standing, because any injury to the Banks is derivative of harm to Reliance Financial Services ("RFS"), the entity to which the Banks made their loans. Defendants argue that the Pension Benefit Guaranty Corporation ("PBGC"), Woodward, and Howard lack standing for the same reason, incorporating by reference the standing arguments contained in the Banks' opening brief.

Reliance Group Holdings ("RGH") is a Delaware corporation. (Dell Affirm., Ex. 23, at Ex. 21.1.) Therefore, Delaware law applies to determine whether the Banks' claims are derivative. *Hart v. General Motors Corp.*, 129 A.D.2d 179, 182-183 (1st Dep't 1987).

Under Delaware law, in order to determine whether Plaintiff's claims are derivative or individual, the

> court should look to the nature of the wrong and to whom the relief should go. The stockholder's claimed direct injury must be independent of any alleged injury to the corporation. The stockholder must demonstrate that the duty breached was owed to the stockholder and that he or she can prevail without showing an injury to the corporation.

Tooley v. Donaldson, Lufkin, & Jenrette, Inc., 845 A.2d 1031, 1039 (Del. 2004). The court must consider "(1) who suffered the alleged harm (the corporation or the suing stockholders, individually); and (2) who would receive the benefit of any recovery or other remedy (the corporation or the stockholders, individually)." *Id.* at 1033; *Yudell v. Gilbert*, 99 A.D.3d 108, 114 (1st Dep't 2012) (adopting the *Tooley* test for distinguishing between direct and derivative claims). "[T]he direct/derivative distinction [does] not vary because the claim was asserted by a creditor instead of a stockholder." *North Am. Catholic Educ. Programming Found., Inc. v. Gheewalla*, 2006 WL 2588971, *11 n.100, 2006 Del. Ch. LEXIS 164, *50 n.100 (Del. Ch. 2006), *aff'd* 930 A.2d 92 (Del. 2007).

As a preliminary matter, the First Amended Plans of Reorganization of RFS and RGH, under chapter 11 of the Bankruptcy Code ("RFS Plan" and "RGH Plan," respectively), assigned creditor claims to RGH, including claims of the Banks, the PBGC, and Woodward and Howard. (Affirmation of William B. Flemming ("Flemming Affirm.") Ex. 154 §§ 5.2(b) and 5.4(b), and Ex. 157 §§ 5.5(b), 6.3, 6.6, 10.6, 12.2, and 12.3; *see also* Disclosure Statement for the RGH Plan, Flemming Affirm., Ex. 156 at 60, 65, and 96.) The RFS and RGH Plans were confirmed by the United States Bankruptcy Court for the Southern District of New York on January 25, 2005 (effective April 22, 2005) and November 7, 2005 (effective December 1, 2005), respectively ("Confirmation Orders"). (Flemming Affirm., Exs. 155 and 158.) Under the RGH Plan, causes of action assigned to RGH "shall be deemed assigned to the Liquidating Trust and become Trust Property, to be managed by the Liquidating Trust. Upon such assignment, the Liquidating Trust shall obtain all rights to litigate such Causes of Action." *Id.*, Ex. 157, § 10.6.

As stated by the Court of Appeals, the Liquidating Trust "is the successor of RGH," and "the assets of RGH's bankruptcy estate vested in the Trust," including the "claims of the bankruptcy estate's creditors, who are the beneficiaries of any recoveries from [defendants]." *RGH Liquidating Trust*, 17 N.Y.3d at 407. In short, the creditor claims were assigned to RGH. RGH, in turn, assigned those claims to Plaintiff, and

Plaintiff now asserts them directly. Thus, there are no derivative claims, and Defendants fail to make a prima facie showing that Plaintiff lacks standing. *Condren, Walker & Co., Inc. v. Portnoy*, 48 A.D.3d 331, 331 (1st Dep't 2008) ("[a]n assignee stands in the shoes of its assignor, subject to all the equities and burdens attached to the property acquired").

In any event, Plaintiff claims that, had Defendants properly disclosed the financial condition of Reliance, the Banks would have: "exercised their rights under the Credit Agreement to declare the loans due and payable and terminate all loan commitments to RFS" (Am. Compl. ¶ 44); sold "the collateral that they had received in exchange for granting the loans to RFS, shares of RIC stock, for cash that could have been applied to satisfy its loans" (*id.*); and refused to extend the maturity date of the existing loans to August 31, 2000. *Id.* ¶ 45. These allegations show harm to the Banks that is distinct from RGH and RFS. If anything, the Banks' alleged injury benefitted RFS, as RFS used the loan proceeds without repaying the Banks. The Banks, therefore, would receive the benefit of any recovery, and these facts give rise to direct claims.

However, certain of Plaintiff's allegations give rise to derivative claims. Plaintiff maintains that RGH distributed funds to persons other than the Banks, that certain of RIC's investments could have been liquidated, and that RIC could have avoided underwriting losses from policies written after March 1, 2000 – all of which could have generated funds to repay the loans. Reliance's expenditures and missed stock sale opportunities resulted in harm to RIC and RGH, which are also the entities that would receive the benefit of any recovery or remedy. *Yudell*, 99 A.D.3d at 114; *Tooley*, 845 A.2d at 1035. Therefore, Plaintiff fails to show any "direct injury" that is "independent of any alleged injury to the corporation" with respect to these allegations, and, therefore, Plaintiff lacks standing to assert these derivative claims. *Tooley*, 845 A.2d at 1039.

For the foregoing reasons, Defendants' motion for summary judgment dismissal, based upon Plaintiff's lack of standing, is granted with respect to Plaintiff's allegations that Reliance incurred expenditures and missed stock sale opportunities that could have generated funds to repay the loans, and is otherwise denied.

B. *Res Judicata*

Defendants next argue that Plaintiff's claims are barred by res judicata, because Plaintiff failed to sufficiently identify the fraud claims in the RGH Plan, RGH's "Disclosure Statement Under 11 U.S.C. § 1125" with respect to the RGH Plan ("RGH Disclosure Statement"), or the RGH Plan schedules. Defendants rely upon *Sure-Snap Corp. v. State St. Bank & Trust Co.*, 948 F.2d 869 (2d Cir. 1991), which has been interpreted by some courts as "impliedly recogniz[ing] that . . . , the right to bring the subsequent litigation must be specifically reserved in the confirmed plan." *Tracar, S.A. v. Silverman*, 266 B.R. 273, 277-278 (E.D.N.Y. 2000) (stating that "[t]he majority of courts that have examined this issue have held that for this exception to apply, the plan must expressly reserve the right to pursue *that particular claim* post-confirmation and that a blanket reservation allowing for an objection to *any claim* is insufficient") (emphasis in original); *but see Futter Lumber Corp. v. Duffy*, 473 B.R. 20, 32 (E.D.N.Y. 2012) (referring to the *Sure-Snap* decision as an "inferred strict approach" that "has not been explicitly adopted by the Second Circuit," and stating that "district and bankruptcy courts within the Second Circuit have not uniformly followed this interpretation of *Sure-Snap*").

"Where the judgment to be given preclusive effect is made in a Federal forum the scope of that judgment, including the applicability of principles of res judicata and collateral estoppel, are governed by Federal law." *Jerome J. Steiker Co. v. Eccelston Props.*, 156 Misc.2d 308, 313 (Sup. Ct. N.Y. Cty. 1992).

Under Section 1141(a) of the Bankruptcy Code:

> the provisions of a confirmed plan bind the debtor and all other parties to a bankruptcy proceeding. A confirmed plan, therefore, constitutes a final judgment on the merits entitled to preclusive effect under the doctrine of *res judicata*. Accordingly, a debtor is precluded from asserting any claims post-confirmation that are not preserved in its plan. However, where the right to pursue litigation is reserved in a plan, *res judicata* will not prevent a debtor from subsequently pursuing those claims.

Goldin Assoc., L.L.C. v. Donaldson, Lufkin & Jenrette Securities Corp., 2004 WL 1119652, *2-3, 2004 US Dist LEXIS 9153, *11-12 (S.D.N.Y. 2004) (internal quotation marks and citations omitted). A majority of courts have held that, for this exception to apply, the reservation must identify with some specificity what claims it intends to preserve and against whom those claims are asserted. *Id.*

The parties do not dispute that, in order to determine whether Plaintiff has properly reserved a claim, the Court must review the RGH and RFS Plans, RGH's Disclosure Statement and schedules, as well as the Confirmation Orders. Here, the RGH and RFS Plans and Disclosure Statements provide that "nothing in the Plan shall release the current and former . . . financial advisors [and] accountants . . . of the Debtor and RFSC, in each case with respect to any act, omission, transaction, event or other occurrence taking place prior to the Petition Date [of June 12, 2001]." RGH Plan, Flemming Affirm., Ex. 157 §§ 1.83, 12.9(c)(i); RFS Disclosure Statement, Flemming Affirm. Ex. 156, at 76; RFS Plan, Flemming Affirm., Ex. 154, § 14.4(c)(i).

The assets transferred by RGH to Plaintiff included "Causes of Action held by the Debtor, the Estate or either Committee and not subject to release under Section 12.9 of the Plan (including Causes of Action assigned to RGH pursuant to the RFSC Plan) . . . ." (RGH Disclosure Statement, at 59; RGH Plan, § 10.6; RGH Confirmation Order, at LL.) Moreover, Defendants do not dispute that a "Joint Tortfeasor Release" was included as an exhibit to a "D&O Settlement" agreement approved by the Bankruptcy Court on April 7, 2005 (RGH Plan, § 1.36), and that the D&O Settlement was included as an appendix to the RGH Plan. *Id.*, §§ 1.85, 15.13. The "Joint Tortfeasor Release" defined "the Liquidator, RIC, RGH, and RFSC" as the "Releasors," and stated, in pertinent part:

> [i]t is expressly understood and agreed that the Releasors are not waiving or releasing any claim that each or all of them has, have or may have against Deloitte & Touche LLP and/or Jan A. Lommele including the Liquidator's claims set forth in Koken v. Deloitte & Touche LLP, et al., 734-MD-2002 (Pa. Commonwealth Court (the "Deloitte Action").

(Fleming Affirm., Ex. 143, at 1.) The "Deloitte Action" was commenced by M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania, in her capacity as Liquidator of RIC, against Deloitte and Lommele as Defendants, and that action was based upon essentially the same factual allegations as the instant action.

In short, even under the "strict approach" of *Sure-Snap*, the RGH and RFS Plans, the RGH Disclosure Statement, and the RGH Confirmation Order demonstrate that the instant action was specifically reserved in the confirmed plan, because these documents name Defendants and provide the legal and factual bases for the reserved claims. *Futter Lumber Corp.*, 473 BR at 28. Accordingly, Defendants fail to make a prima facie showing that Plaintiff's claims were not preserved in the RGH and RFS Plans, and their motion is denied as to this basis.

III. Fraud Claims Asserted on Behalf of the Banks (mot seq 021)

Defendants present several arguments for dismissal of Plaintiff's fraud claims. First, Defendants contend that Plaintiff cannot establish the elements of proximate cause and reliance. Further, Defendants also argue that Plaintiff cannot pursue claims concerning creditors not identified in the amended complaint. These arguments will be addressed in turn below.

A. *Fraud and Proximate Cause*

"In order to recover for fraud, plaintiffs must show a representation of material fact, the falsity of that representation, knowledge by the party who made the representation that it was false when made, justifiable reliance by the plaintiff, and resulting injury." *Pope v. Saget*, 29 A.D.3d 437, 441 (1st Dep't 2006). As an element of the fraud causes of action, Plaintiff must demonstrate that Defendants' "misrepresentations were the direct and proximate cause of the claimed losses. A fraudulent misrepresentation is a legal cause of a pecuniary loss resulting from action or inaction in reliance upon it if, but only if, the loss might reasonably be expected to result from the reliance." *MBIA Ins. Corp. v. Countrywide Home Loans, Inc.*, 87 A.D.3d 287, 295 (1st Dep't 2011) (internal quotation marks and citations omitted); *see also Laub v. Faessel*, 297 A.D.2d 28, 31 (1st Dep't 2002) ("there [must] be some reasonable connection between the act or omission of the defendant and the damage which the plaintiff has suffered"). While "[t]he issue of '[p]roximate cause is a question of fact for the jury where varying inferences are possible,'" *Sweeney v. Bruckner Plaza Assoc.*, 57 A.D.3d 347, 348 (1st Dep't 2008), a fraud claim is subject to summary judgment dismissal where no triable issue of fact exists with respect to proximate cause. *Safchik v. Prudential Sec.*, 233 A.D.2d 383, 384 (2d Dep't 1996).

Defendants rely heavily upon *Starr Foundation v. American International Group, Inc.*,76 A.D.3d 25, 28 (1st Dep't 2010). In *Starr Foundation*, the plaintiff refrained from selling a large block of American International Group's ("AIG") common stock, based upon AIG's alleged public misrepresentations concerning the risks associated with its credit default swap portfolio. The plaintiff claimed that it would have divested its ownership interests but for AIG's misrepresentations, but instead held the stock while its value declined. The First Department affirmed the trial court's dismissal of the complaint, stating:

> [i]f the case were to go to trial, to establish liability and damages the [plaintiff] would be required (in addition to proving the fraudulent nature of the statements complained of) somehow to come forward with a nonspeculative basis for determining how accurate disclosure of the risk of the [credit default swap] portfolio beginning in August 2007—and such disclosure's hypothetical effect on the market at that time—would have affected the [plaintiff's] decision to sell or retain its AIG stock and the amount it would have received for the stock it hypothetically would have sold.

Id. at 27. In *Starr Foundation*, the plaintiff continued to hold its remaining AIG stock, even after the alleged fraud was exposed and the share price dropped. *Id.* at 30. The Court stated that the "speculative nature" of the plaintiff's claim was underscored by the testimony of the plaintiff's president, who stated that he could not speculate as to whether the plaintiff would have sold all of its AIG stock had it known about the alleged fraud earlier. *Id.* The Court concluded that "neither would it be appropriate for a jury to speculate on the answer to this question." *Id.*

B. *Defendants' Prima Facie Showing on Proximate Cause*

Defendants argue that their reports did not proximately cause Plaintiff's loss, since there is no evidence that the Banks would have taken any of the actions alleged in the pleading but for Defendants' alleged misrepresentations. These actions include: (1) exercising their rights under the Credit Agreement to declare the loans due and payable and terminate all loan commitments to Reliance Financial Services; (2) refusing to extend the loans from March 31, 2000 to August 31, 2000; (3) selling the collateral that secured the loans; (4) recommending that Reliance sell its Financial Products Division and its Excess and Surplus Lines Division, to generate funds to repay the loans; and, (5) contacting Reliance's independent audit committee and/or state insurance regulators. (Am. Compl. ¶¶ 44-47.) Each of these allegations is discussed below.

1. Declaring the Loans Due and Terminating RFS Loan Commitments

Plaintiff alleges that, had the Banks known that the financial reports were overstated, they would have exercised their rights under the Credit Agreement to declare the loans due and payable on the original maturity date of March 31, 2000, terminating all loan commitments to Reliance Financial Services. However, Defendants submit the Banks' testimony, stating that they never called due their loans even after discovering Reliance's true financial condition. (Affirmation of Michael J. Dell ("Dell Affirm."), Ex. 13 at 29, 67; Ex. 14 at 129; Ex. 15 at 110-111; Ex. 16 at 17; Ex. 17 at 96-97; Plaintiff's Rule 19-a Response ¶ 91.) In February 2000, RFS informed the Banks that it could not repay the loans, and Reliance sought a five-month extension for repayment. Thereafter, the Banks agreed to extend the maturity date of the loans from March 31, 2000 to August 31, 2000, because failing to do so would have caused a downgrade in Reliance's ratings, making it difficult for Reliance to write new insurance and repay the loans. (Dell Affirm., Ex. 6 at 32-33, 48-50, 56-57, 87; Ex. 7 at 21, 30-33, 55-57; Ex. 9 at 40, 47; Ex. 10 at 0054; Ex. 11 at 4024; Ex. 18 at 23-24; Ex. 19 at 398, 404; Ex. 20 at 5929-5930; Ex. 21 at 3258.) The Banks' testimony, internal memoranda, and credit extension applications all indicate that the Banks "[did] not have any viable alternative" other than to agree to RFS's extension request." *Id.*, Ex. 7 at 56-57; Ex. 9 at 47; Ex. 11 at 4025; Ex. 17 at 29-30, 57; Ex. 18 at 23-24; Ex. 19 at 404; Ex. 20 at 5929-5930; Ex. 21 at 3258. The Banks testified that, if Reliance's true financial condition were revealed in March of 2000 – indicating that the company's finances were far worse than actually reported by Defendants – the ratings agencies would have further downgraded Reliance, making it more difficult for the Banks to be repaid. *Id.*, Ex. 7 at 32-33; Ex. 17 at 29-30, 57.

The Banks also did not call due their loans in August 2000, when Reliance announced that: it was increasing loss reserves by $460 million; it could not repay the loans; it was further downgraded to "B"; it was unable to write new business and operating in a run-off mode; the sale of Reliance to Leucadia National Corporation fell through in July of 2000; and it was considering a bankruptcy filing. (Dell Affirm. Ex. 6 at 73-74, 78, 89-90, 95; Ex. 7 at 80, 83; Ex. 13 at 29-30, 53-54; Ex. 14 at 88-90; Ex. 29 at 3366-3367; Ex. 31 at 0365; Ex. 43 at 2; Ex. 44 at 0065.) Instead, the Banks agreed to waive Reliance's default under the Credit Agreement and to further extend the loan maturity date to November 10, 2000. The Banks acknowledged the possibility that regulators could place Reliance in rehabilitation or liquidation, and that the "regulators are likely to prohibit the upstreaming of any normal dividends, i.e., from the insurance subsidiaries to our Borrower [RFS]." *Id.*, Ex. 29 at 3367; Ex. 13 at 54-55.

The Banks testified that, in August 2000, Reliance was not operating as a going concern, but rather, was operating in a run-off/liquidation mode. (Dell Affirm. Ex. 4 at 90-91; Ex. 7 at 85; Ex. 14 at 67-68, 85-86; Ex. 31 at 361.) On October 23, 2000, Reliance announced that it was increasing its loss reserves by approximately $332 million, with the aggregate loss reserve increase now totaling over $800 million. (Dell Affirm. Ex. 13 at 67-68; Ex. 14 at 98-99, 127-128, 154; Ex. 40 at 545-546; Ex. 41 at 4; Ex. 49; Ex. 50; Ex. 51, at 87; Ex. 124; Ex. 125.) This loss reserve increase reduced Reliance's surplus to approximately $500 million, which was $300 million less than the minimum required under the Credit Agreement. Credit Agreement, § 6.2.2(a)(i). Even after the additional loss reserve increase, PriceWaterhouseCoopers ("PWC") informed the Banks that the loss reserves were understated by $240 million. (Dell Affirm. Ex. 13 at 67-68; Ex. 14 at 98-99, 127-128, 154; Ex. 40 at 545-546; Ex. 41 at 4; Ex. 49; Ex. 50; Ex. 51 at 87.) Also on October 23, 2000, the Banks learned of RGH and RFS's plan to file bankruptcy and sought to avoid Reliance being placed into liquidation. (Dell Affirm., Ex. 51 at 87-88.)

Reliance again defaulted under the Credit Agreement when it failed to repay the loans on the extended maturity date of November 10, 2000 (Credit Agreement, § 7.1.1), but the Banks continued to forebear from calling the loans due, with hopes of restructuring the debt. (Dell Affirm. Ex. 4 at 100-101, 116-119; Ex. 17 at 96-97; Ex. 18 at 38-39; Ex. 41 at 2; Ex. 50 at 1008; Ex. 52.) Also in November 2000, the Banks learned that the Pennsylvania Insurance Department estimated Reliance's surplus as approximately $500 million. (Dell Affirm. Ex. 13 at 68; Ex. 41 at 4, 5.)

Section 7.3 of the Credit Agreement permitted the Banks, upon an event of default, to "declare all or any portion of the outstanding principal amount of the Loans to be due and payable," but the agreement required notice to RFS "upon direction of the Required Lenders." (Credit Agreement, Dell Affirm. Ex. 2 at 82.) The Credit Agreement defined "Required Lenders" as "Lenders having a then aggregate Combined Percentage of at least 66 - 2/3%." *Id.* § 1.1, at 24. The foregoing evidence makes a prima facie showing that *none* of the Banks, let alone 66% of the Banks, sought to declare the loans due and payable at any time, even after Reliance's true financial condition became known.

The evidence also shows that RFS could not repay the loans without a dividend from Reliance Insurance Company ("RIC"). (Dell Affirm. Ex. 4 at 58; Ex. 7 at 69-70; Ex. 9 at 48-49; Ex. 13 at 55, 109; Ex. 18 at 40.) However, the Pennsylvania Insurance Department testified that, if RIC had reported that its surplus was $1 billion less than what RIC actually reported in March of 2000, the Pennsylvania Insurance Department would not have allowed RIC to pay any dividends to RFS. *Id.*, Ex. 172, at 8-11, 38-39. The Pennsylvania Insurance Department would not have permitted RIC to upstream any payments to RFS or RGH "unless and until [it was satisfied] that the policyholders could be paid in full." *Id.* at 20; *see also* Fleming Affirm., Ex. 43 ¶¶ 23-26 (Pennsylvania Insurance Department Deputy Insurance Commissioner's verification, stating that, if Reliance reported a surplus of $268 million instead of $1.2 billion, the Pennsylvania

Insurance Department would not have permitted intercompany payments, tax payments, or loans). The Banks acknowledged that the Pennsylvania Insurance Department would not have permitted RIC to pay dividends to RFS until RIC's loss reserves were sufficient to satisfy policyholder claims. (Dell Affirm., Ex. 7 at 69-70; Ex. 17 at 36-37; Ex. 27 at 278; Ex. 29 at 3367; Ex. 4, at 73; Ex. 47 at 62.)

As of September 30, 2011, however, the Insurance Commissioner of the Commonwealth of Pennsylvania, the statutory liquidator of RIC, reported that RIC's net deficit in policyholder surplus was \$3.6 billion.[3] (Dell Affirm. Ex. 79 at 4 and Ex. B; Ex. 172 at 17-19, 30.) The Pennsylvania Insurance Department also testified that policyholder claims (and federal income tax and estate expenses) are entitled to priority payment before dividends are paid to RFS. *Id.* Ex. 79 at 19. Although RIC made three payments to RGH after March 2000, an amount totaling \$91.4 million, the Pennsylvania Insurance Department testified that if RIC's surplus were accurately reported at \$200 million instead of \$1 billion, the Pennsylvania Insurance Department would not have permitted RIC to make the \$91.4 million in payments to RGH. *Id.* Ex. 172 at 11-12. In fact, in June of 2000, the Pennsylvania Insurance Department rejected Reliance's request to pay a \$200 million dividend to RGH, even though RIC had (erroneously) reported its

[3] The Pennsylvania Insurance Department testified that "policyholder surplus" is "the cushion that insurance companies are required to have in excess of their liabilities, which includes their potential payout of their claims to policyholders . . . as they come due." (Dell Affirm. Ex. 172 at 18.)

surplus as $1.2 billion. *Id.* at 12. Thus, if RIC's loss reserves were accurately stated in the reports prepared by Defendants, after satisfying policyholder claims, any attempt by RFS to declare the loans due and payable would have been fruitless, because there were no funds left to upstream to RFS.

Like the plaintiff in *Starr Foundation*, the Banks "remained in possession of the true value of the [loans], whatever that value may have been at any given time," and any decline in the value of the loans or RFS's ability to repay them was caused by RIC's massive losses, which "would have been incurred regardless of any earlier misrepresentation [defendants] made concerning [RIC's loss reserves]." *Starr Found.*, 76 A.D.3d at 28-29 ("the paper 'loss' the [plaintiff] seeks to recover in this action was caused by the underlying business decision of [defendant's] management to build up the CDS portfolio on which the losses reported in early 2008 were sustained, not by the earlier alleged misrepresentations forming the basis of the [plaintiff's] complaint"). For the foregoing reasons, Defendants have made a prima facie showing that the Banks would not have called due their loans, and that even if they did, the Pennsylvania Insurance Department would not have permitted RIC to make any payments to RFS, thereby preventing RFS from repaying the loans.

2. Refusing to Extend the Loans

Plaintiff alleges that the Banks "would not have agreed to extend the maturity date of the existing loans from March 31, 2000 to August 31, 2000 but for [Defendants'] false representations about Reliance's financial condition." (Am. Compl. ¶ 45.) However, RGH's Securities and Exchange Commission Form 10-K, for the period ending December 31, 1999, which included Defendants' audit report, was not released until March 30, 2000 (*id.*, Ex. 23), and Lommele's statement of actuarial opinion was dated February 25, 2000. *Id.* Ex. 24. The Banks executed the amendment to the Credit Agreement, extending the maturity date of the loans, by February 22, 2000 (the amendment itself is dated February 1, 2000). (Dell Affirm., Ex. 22; Ex. 6 at 59-61; Ex. 7 at 20; Ex. 18 at 64-65.) Thus, Plaintiff's allegation is negated by the fact that the Banks agreed to extend the loan *before* Defendants issued their reports.

3. Selling Collateral that Secured the Loans

Plaintiff alleges that the Banks would have sold their stock collateral in Reliance Insurance Company, using the proceeds to satisfy the loans, pursuant to rights granted under the Pledge Agreement. (Am. Compl. ¶ 44.) The Pledge Agreement permitted the sale of the RIC stock collateral "[i]f any Notice of Acceleration shall be in effect (and subject to Section 1402 Filing and Approval)." (Pledge Agreement, Dell Affirm. Ex. 3 §

6.1.) However, none of the evidence before the court indicates that an acceleration notice was in effect. Moreover, the Pledge Agreement defined "Section 1402 Filing and Approval" as, "relative to any action to be taken by the Stock Collateral Agent with respect to Pledged RIC Shares, the filing pursuant to section 1402 of the Insurance Company Law . . . with, and the approval by, the Pennsylvania Commissioner required in connection therewith." *Id.* at 5; Ex. 70 (November 12, 1999 letter from the Pennsylvania Insurance Department, stating that, under the Pledge Agreement, upon an event of default, "the Trustee and the Secured Parties cannot take control of the stock without having first made the filing required under Section 1402 . . . and secured the approval of the Insurance Commissioner").

Here, none of the evidence shows that the Banks sought the Pennsylvania Insurance Department's approval to foreclose on RIC's stock or that any such request for approval would have been granted. To the contrary, Defendants' prima facie showing establishes that the Banks never sought to foreclose on the collateral, notwithstanding RFS's numerous defaults and mounting loss reserve deficits. *See e.g.* Dell Affirm. Ex. 27 at 277 (Bank's August 8, 2000 credit risk memorandum, indicating that "[i]t is unlikely that the Bank Group will be able to foreclose on the stock due to the regulatory restrictions by the Department of Insurance"); Ex. 7 at 70 (Bank witness testifying that the Banks were "prevented" from foreclosing on RIC's stock). Nor is there any evidence that the Pennsylvania Insurance Department would have approved the sale of RIC stock; and even if the Pennsylvania Insurance Department were to consider such approval, the evidence shows that efforts were made, unsuccessfully, to sell RIC before and after the issuance of Defendants' inflated financial reports. (Dell Affirm. Ex. 4 at 64-65, 79; Ex. 6 at 76; Ex. 7 at 53-54, 70-71; Ex. 9 at 119; Ex. 11 at 4024; Ex. 13 at 58-59, 61-62; Ex. 14 at 92; Ex. 17 at 60-61; Ex. 42 at 73.) The evidence makes clear that it would have been even more difficult to sell the RIC stock if the reports prepared by Defendants indicated that RIC's financial condition was worse than what was actually reported. *Id.* Ex. 4 at 81; Ex. 17 at 29; Ex. 20 at 5930.

Moreover, Plaintiff's interrogatory response stated that Defendants' failure to act in accordance with their professional obligations:

> ensured that when KKR, in connection with its potential investment in the Company, discovered Reliance's true financial condition, and Leucadia, in connection with its potential purchase of the lender banks' collateral, discovered that Reliance's financial statements were deceptive and misleading, each would abandon those transactions following their respective due diligence on the Company.

(Dell Affirm. Ex. 168 at 7.) Plaintiff implicitly concedes that Defendants' accurate reporting of RIC's financial condition would have deterred potential investments in, and the purchase of, RIC. Thus, Defendants make a prima facie showing that the Banks would not, and, in fact, could not, have taken steps to sell the RIC stock held as collateral under the Pledge Agreement.

4. Selling Financial Products and its Excess and Surplus Lines Divisions

Plaintiff alleges that the Banks could have "recommend[ed] to Reliance that it sell assets . . . to protect their loans, including . . . Reliance's Financial Products Division . . . and its Excess and Surplus Lines Division," generating $300 - $500 million that could have been used to repay the loans. (Am. Compl. ¶ 46.) As a preliminary matter, there is no factual basis in the record that the Banks would or could have recommended that Reliance sell these assets, or that Reliance would have consented to such a request. In response to Defendants' interrogatories, Plaintiff failed to identify "when, to whom and at what price . . . Reliance would have sold its Financial Products and Excess and Surplus Lines Divisions" (Dell Affirm. Ex. 168 at 7-8), and, as a result, any purported sale of Reliance's assets is "'undeterminable and speculative.'" *Starr Found.*, 76 A.D.3d at 28. As discussed above, if RIC's true financial condition were disclosed, it is even less likely that the Banks would have recouped their loans because of the increased difficulty of selling RIC's assets as their value diminished. Furthermore, even assuming for the moment that these assets could have been sold, as discussed above, the evidence establishes that the Pennsylvania Insurance Department would not have permitted the sale proceeds to be upstreamed to RFS to repay the loans if RIC's surplus were reported to be $1 billion less. Accordingly, Defendants have made a prima facie showing refuting Plaintiff's allegation concerning the sale of the two Reliance divisions.

5. Contacting Reliance's Independent Audit Committee and/or State Insurance Regulators

Plaintiff next alleges that, based upon Defendants' misrepresentations, the Banks did not take measures to prevent the depletion of assets, such as contacting Reliance's independent audit committee and/or state insurance regulators. (Am. Compl. ¶ 47.) According to Plaintiff, these entities could have stopped Reliance Insurance Company's accumulation of additional liabilities generated from RIC's continued writing of insurance policies, and prevented millions of dollars in operational costs. *Id.* Plaintiff claims that the Banks also could have forced the timely sale of Reliance's assets, generating cash to repay the loans. *Id.*

However, the evidence demonstrates that the Banks sought to avoid regulatory involvement – involvement which would have become more imminent if RIC's surplus were reported to be $1 billion less. (Dell Affirm., Ex. 7, at 77; Ex. 9, at 51-52; Ex. 13, at 29-30, 55, 57-58, 91-92, 94-96; Ex. 14, at 58-59; Ex. 16, at 16-17; Ex. 17, at 34; Ex. 42, at 73; Ex. 43, at 2; Ex. 172, at 9-12.) Nor does any of the evidence suggest that the Banks would have contacted Reliance's audit committee, as they failed to do so even after RIC's ratings were downgraded and the company's dire financial condition was fully exposed. (Dell Affirm., Ex. 4, at 25; Ex. 6, at 20, 94; Ex. 7, at 71; Ex. 9, at 28; Ex. 13, at 80; Ex. 15, at 112; Ex. 16, at 14; Ex. 17, at 64; Ex. 18, at 34.) Moreover, as discussed above, the evidence demonstrates that the Banks never sought to compel RIC to stop writing insurance policies, because this would force RIC into run-off and, ultimately, liquidation. The Banks testified that they were aware that Reliance was already cutting costs, and they could not identify anything else RIC could have done to cut costs. (Dell Affirm., Ex. 4, at 86-87; Ex. 9, at 25-26; Ex. 13, at 60-61, 103-104; Ex. 14, at 87; Ex. 15, at 69-70; Ex. 16, at 18; Ex. 17, at 62-63; Ex. 18, at 18.) Nothing in the record indicates that the Banks could have forced the sale of RIC's assets, and, in any event, the Pennsylvania Insurance Department would not have permitted RIC to upstream funds to RFS if RIC's surplus were reduced by $1 billion.

For the foregoing reasons, Defendants make a prima facie showing that their financial reports did not proximately cause the Banks' injury and were not "a substantial factor in inducing the [Banks] to act the way [they] did," and that Plaintiff's allegations are based upon speculation and the mere possibility of causation, further supporting Defendants' motion for summary judgment dismissal. *Curiale v. Peat, Marwick, Mitchell & Co.*, 214 A.D.2d 16, 27 (1st Dep't 1995); *Starr Found.*, 76 A.D.3d at 27, 28; *see also Nicosia v. Board of Mgrs. of Weber House Condo.*, 77 A.D.3d 455, 456 (1st Dep't 2010) (dismissing fraud claim where plaintiff failed to "explain how he relied to his detriment"); *Shea v. Hambros PLC*, 244 A.D.2d 39, 46-47 (1st Dep't 1998) (granting summary judgment dismissal of fraud claim where the plaintiff was not "induced to act [or] refrain from acting to his detriment by virtue of the alleged misrepresentation or omission [internal quotation marks omitted]"); *Silva v. Village Sq. of Penna*, 251 A.D.2d 944, 945 (3d Dep't 1998) (affirming summary judgment dismissal where "the trier of fact would be required to base a finding of proximate cause upon nothing more than speculation").

C. *Plaintiff's Rebuttal on Proximate Cause*

In opposition, Plaintiff argues that evidence of the Banks' inaction, in reliance upon Defendants' misrepresentations, establishes loss causation. In support of its argument, Plaintiff cites to footnote 5 in *Starr Foundation*, where the court noted that "the out-of-pocket rule is not an obstacle to a creditor's claim that it was fraudulently induced to forbear from taking steps to collect a debt." 76 A.D.3d at 33 n.5 (citing *Hotaling v. Leach & Co.*, 247 N.Y. 84 (1928) and *Foothill Capital Corp. v. Grant Thornton, L.L.P.*, 276 A.D.2d 437, 438 (1st Dep't 2000)); *see also Eden Rock Fin. Fund, L.P. v. Gerova Fin. Group LTD.*, 34 Misc.3d 1205(A), *4, 2011 NY Slip Op 52431(U) (Sup. Ct. N.Y. Cty. 2011) (quoting footnote 5 from *Starr Foundation*).

1. Forbearance of Collection Efforts

Here, the evidence establishes that the Banks intentionally forewent collection efforts, repeatedly excusing events of default and granting maturity date extensions, with hopes of avoiding regulatory intervention, which would have materialized much sooner if Reliance Insurance Company's surplus were reported to be $1 billion less.

Footnote 5 from *Starr Foundation* does not vitiate the requirement of loss causation as an element of Plaintiff's fraud claim. At trial, Plaintiff would be unable to "come forward with a nonspeculative basis for determining how accurate disclosure of [Reliance's financial condition] —and such disclosure's hypothetical effect on the market at that time—would have affected the [Banks'] decision to sell or retain [the loans]." *Starr Found.*, 76 A.D.3d at 27. The overstatement of loss reserves did not cause the Banks to forbear from taking steps to collect the loan. The evidence makes clear that the Banks were unable to collect the debt regardless of any overstatement of RIC's loss reserves. In this regard, Defendants' reliance upon *Starr Found.* does not blur the distinction between proximate cause and damages, as Plaintiff argues (9/13/12 Hearing Tr., at 94). Rather, *Starr Foundation* underscores that Plaintiff's arguments and assertions are based upon speculation.

To the extent that Plaintiff seeks to "recover the fair market value loss on the [loans] that it would have sold in the absence of [Defendants'] fraud," and "to restore itself to the position it occupied without the fraud," *Starr Found.*, 76 A.D.3d at 46 (Moskowitz, J., dissenting), those efforts are defeated by the fact that the Banks' investment had no value without the fraud. If anything, the evidence shows that the Banks intentionally postponed debt collection in an effort to salvage their investment, an investment which would have evaporated if surplus were reported to be $1 billion less than the amount Plaintiff alleges was actually reported. Thus, the Banks' damages were not caused by understated loss reserves. Instead, it appears that Defendants' reports gave life – however brief – to a dying investment.

Plaintiff claims that, in 2000, when the Banks were monitoring Reliance, they were aware that Reliance was selling assets and attempting a complete sale to Leucadia, with the proceeds of these transactions being used to repay the loans. Plaintiff argues that the Banks' unsuccessful collection efforts, and their inaction generally, were caused by Defendants' fraud. In support of this argument Plaintiff cites to: *In re Refco Sec. Litig. v. Sugrue*, 2012 WL 607612, 2012 US Dist LEXIS 25661 (S.D.N.Y. 2012); *AUSA Life Ins. Co. v. Ernst & Young*, 206 F.3d 202 (2d Cir. 2000) (*AUSA Life I*); and *Sterling Natl. Bank v. Ernst & Young LLP*, 21 Misc.3d 1141(A), 2008 NY Slip Op 52473(U) (Sup. Ct. N.Y. Cty. 2008), *aff'd* 62 A.D.3d 584 (1st Dep't 2009).

This argument adds nothing new to Plaintiff's previous argument, and the cases cited by Plaintiff are distinguishable on their facts. *In re Refco Securities Litigation* held that PriceWaterhouseCoopers could not have aided and abetted "the Refco fraud" because, "by the time PWC engaged in its advisory work, Refco and RCM were already 'hopelessly insolvent.'" 2012 WL 607612, *4, 2012 US Dist LEXIS 25661, *38. The court reasoned that, "even absent PWC's actions, plaintiffs had no way to prevent the loss of their assets deposited at Refco before PWC assisted the Refco fraud. Refco and RCM were insolvent, and a run on the bank would have occurred regardless of whether PWC enabled the Refco fraud to continue." *Id.* at *5, *41. Thus, *In re Refco Securities Litigation* supports dismissal of Plaintiff's fraud claims, because regardless of Defendants' financial reports, the Banks had no way to prevent the loss of their investment.

Plaintiff cites to *AUSA Life I* in support of its statement that causation is established where the auditor's fraud prevented the plaintiff-investor from exercising the right to accelerate payment on its note, regardless of whether the plaintiff would have actually demanded accelerated payment. (Pl.'s Opp. Br. at 69.) Upon close examination, however, *AUSA Life I* and its progeny do not support Plaintiff's argument. In *AUSA Life I*, a group of insurance companies invested approximately $150 million in the securities of JWP, Inc., pursuant to note purchase agreements. In purchasing the notes, the insurance companies relied upon JWP, Inc.'s production of past and ongoing financial statements, which were certified by the defendant accounting firm, Ernst & Young. The financial statements were consistently inaccurate, and after a series of aggressive acquisitions, JWP, Inc. was unable to continue paying interest on the notes. JWP, Inc. defaulted and was placed in involuntary bankruptcy. The insurance companies sued Ernst & Young for fraud, and after a bench trial, the district court dismissed plaintiffs' fraud claim for failure to show loss causation. Specifically, the trial court concluded that JWP, Inc.'s insolvency and default on the notes were caused by the financial troubles of one of the companies it acquired, and a market downturn generally, not because of "'the fiscal infirmities concealed by JWP's annual reports.'" *AUSA Life Ins. Co. v. Ernst & Young*, 119 F. Supp. 2d 394, 396 (S.D.N.Y. 2000).

On appeal, the Second Circuit issued a three-opinion decision, vacating and remanding on the issue of loss causation, because the circumstances permitted varying inferences as to whether the investors would have waived JWP Inc.'s defaults and allowed the aggressive acquisition strategy to proceed had JWP, Inc. known the company's true financial condition. On remand, the trial court again dismissed the complaint, finding that "plaintiffs' loss on their investments in JWP's notes was not a foreseeable result of [Ernst & Young's] complicity in JWP's misrepresentations but of post-audit developments that could not have been anticipated." *Id.* at 407.

The plaintiffs again appealed on the issue of loss causation. The Second Circuit acknowledged that its "previous decision with respect to this litigation generated three divergent opinions, each therefore without binding precedential effect." *AUSA Life Ins. Co.*, 39 Fed App'x 667, 669 (2d Cir. 2002) (*AUSA Life II*). In any event, in *AUSA Life II*, the Second Circuit made clear that "the plaintiffs were required to demonstrate that, with the information available at the time, it is more probable than not that they would have exercised their options in a way that would have ultimately obviated their losses." *Id.* at 672. The Court held that the plaintiffs failed to satisfy this burden, reiterating its prior conclusion that "what the plaintiffs and JWP would have done had the defendant revealed the defaults . . . involved pure speculation." *Id.* (reaching same conclusion on "enabling theory" and "forebearance theory"); *see also id.* at 673-674 (rejecting plaintiffs' "'buy and hold' theory," requiring a showing of loss causation). In short, the *AUSA Life I* and *II* decisions are of limited precedential value, and, in any event, do not support Plaintiff's argument in the instant action, especially where the evidence is not subject to varying inferences or conclusions.

Plaintiff cites to *Sterling National Bank*, 21 Misc.3d 1141(A) (Sup. Ct. N.Y. Cty. 2008), in opposition to Defendants' argument that proper disclosure of Reliance's true financial condition would not have resulted in any funds available to pay the Banks. However, in *Sterling National Bank*, the parties presented "conflicting theories and data" on the issue of loss causation, raising factual issues that precluded summary judgment. 21 Misc.3d 1141(A), *5. Here, conversely, Plaintiff submits no evidence to rebut

Defendants' prima facie showing, but rather, Plaintiff relies upon attorney statements contained in Plaintiff's opposition brief, which are insufficient to create an issue of fact. *Zuckerman v. City of New York*, 49 N.Y.2d 557, 563 (1980) (attorney affirmation "without evidentiary value and thus unavailing"); *Katz Park Ave. v. Jagger*, 46 A.D.3d 186, 190 (1st Dep't 2007). Nor does Plaintiff submit a "conflicting theor[y]" that would warrant denial of summary judgment under *Sterling National Bank*. Thus, none of the cases cited by Plaintiff raise a factual issue as to whether the Banks were fraudulently induced to forbear from debt collection efforts.

2. <u>Election Not to Sell Loans in Secondary Market</u>

Plaintiff next argues that the Banks elected not to sell their loans in the secondary market, which in the year 2000 were trading at 71.5 and 51.25 cents on the dollar. According to Plaintiff, some of the Banks sold their loans, and the Banks that did not sell their loans "had calculated that repayment from Reliance's surplus would exceed that market price." (Pl.'s Opp. Br. at 70.) Plaintiff's argument fails to consider how the loan value would be affected by accurate financial reporting. The secondary market may have fetched 71.5 to 51.25 cents on the dollar with a $1 billion overstatement in RIC's surplus. Tellingly, however, Plaintiff concedes that, "[h]ad disclosure of Reliance's true financial condition been disclosed in March 2000, the Company would have already been 'tanked'

. . . ." (Pl.'s Rule 19-a Response to PBGC ¶ 61.) Plaintiff offers no evidence that a secondary market would have existed at all if RIC's financial condition were accurately reported.

Plaintiff concedes that Carl Icahn, "the predominant buyer of Reliance's bank debt . . . immediately ceased all further purchases of bank debt upon learning news of Reliance's negative surplus in late March 2001. (Pl.'s Opp. Br., at 71; Fleming Affirm., Ex. 127.) Plaintiff also conceded in its interrogatory response that, once KKR and Leucadia discovered "Reliance's true financial condition," they would "abandon" their investments in the company. (Dell Affirm., Ex. 168, at 6-7.) In other words, Plaintiff's assertion that the Banks could have sold their loans assumes that the Banks knew RIC's "true financial condition" while the marketplace remained ignorant. The evidence before the court fails to raise a factual issue as to the existence of a secondary market, let alone any damages resulting from the Banks' failure to sell their loans in it. *See Starr Found.*, 76 A.D.3d at 28 (finding lost bargain "undeterminable and speculative," where plaintiff sought "to recover the value it might have realized from selling its shares during a period when it chose to hold, under hypothetical market conditions for AIG stock [assuming disclosures different from those actually made] that never existed").

3. RGH Distributions to Non-Bank Entities

Plaintiff next argues that RGH distributed $120 million to persons other than the Banks, which could have been preserved to repay the loans. Plaintiff also claims the Banks could have liquidated RIC's investments in Symbol Technologies and Land America, which in March 2000 had a market value of $1 billion and could have been used to repay the loans. Plaintiff maintains that the failure to liquidate RIC's investments in these companies deprived the Banks of tax loss carryforwards generated from capital gains, with net after-tax cash value of $126 million that could have been used by RGH to repay the loans. Plaintiff also maintains that RIC incurred $134 million in underwriting losses from policies written after March 1, 2000, which would have been avoided by accurate financial reporting in March 2000.

As discussed above, *see supra* at Section II.A, Plaintiff lacks standing to assert derivative claims concerning Reliance's expenditures and missed stock sale opportunities. However, even if Plaintiff had standing, the evidence refutes these claims. Specifically, Plaintiff fails to explain how the Banks could have stopped Reliance Group Holdings' spending of $120 million or obtained any funds distributed by RGH, as the obligation to repay the loans belonged to Reliance Financial Services, not RGH. Moreover, the evidence demonstrates that RIC upstreamed $91.4 million to RGH in June and July of 2000 (Fleming Affirm., Ex. 150), but the Pennsylvania Insurance Department testified that it would not have permitted this upstreaming if Reliance had properly reported its surplus. (Fleming Affirm., Ex. 43, ¶ 25.) Thus, Plaintiff fails to explain how, if Reliance Insurance Company's financial condition were properly disclosed, RGH would have had the $120 million to spend, and how the Banks could have stopped any such spending.

Plaintiff's spending argument includes $103 million in restructuring charges, through September 30, 2000, and monthly expenses of $2 million for "financial advisors, legal, audit," through RGH's bankruptcy filing in June 2001. (Pl.'s Opp. Br. at 71.) Plaintiff claims that this spending was unnecessary, because Reliance's financial condition had deteriorated to such an extent that restructuring was unnecessary. However, Plaintiff does not dispute that the Banks were aware that Reliance was cutting costs, and could not identify anything more that it could have done to raise capital or reduce expenses. (Pl.'s Rule 19-a Response ¶¶ 130, 132.) Plaintiff also fails to show that RFS had any entitlement to these funds or the ability to use them to repay the loans, or that the Pennsylvania Insurance Department would have permitted these funds to be used for loan repayment. Nor has Plaintiff shown that any restructuring charges could have been avoided but for Defendants' financial misrepresentations.

In addition, Plaintiff fails to submit evidence showing that the Banks could or would have forced RIC to sell its stock holdings in Symbol Technologies and Land

America. Nor does Plaintiff raise a factual issue to rebut Defendants' prima facie showing that the Pennsylvania Insurance Department would not have permitted RIC to upstream proceeds from any stock sales to RFS in order to repay the loans. Plaintiff also fails to explain who would have paid $126 million (in tax loss carryforwards) to RGH or provide a legal basis for the Banks to obtain RGH's funds, as the funds were owed by RFS, not RGH.

The same is true of Plaintiff's argument that $134 million in RIC's underwriting losses from policies written after March 1, 2000 could have been avoided, as Plaintiff fails to explain what the Banks could or would have done to prevent RIC from writing new policies. Nor is there any evidence that preventing RIC from writing new policies would have increased the Banks' recovery on the loans, because RIC's net deficit in policyholder surplus was $3.6 billion, and, in any event, the Pennsylvania Insurance Department would not have permitted RIC to upstream funds to RFS. (Dell Affirm., Ex. 79, at 4 and Ex. B; Ex. 172, at 17-19, 30.)

D. *Conclusion with Respect to the Banks*

For the foregoing reasons, Plaintiff fails to rebut Defendants' prima facie showing that proximate cause is lacking. Accordingly, Defendants' motion for summary judgment is granted, and the Amended Complaint is dismissed with respect to the Banks' claims.

Having dismissed the Amended Complaint on the merits for lack of proximate cause, the court does not address Defendants' remaining arguments that Plaintiff's claims should be dismissed for failure to demonstrate reliance and on grounds of *in pari delicto* and spoliation.

E. *Unidentified Creditors*

The court also notes Defendants' argument that Plaintiff cannot pursue claims concerning creditors not identified in the Amended Complaint, because these claims were already dismissed and because Plaintiff cannot establish reliance with respect to these unidentified creditors. According to Plaintiff, these claims arise as a result of certain Banks assigning or selling their loan participation interests to third parties. As all of Plaintiff's Bank claims are dismissed for lack of proximate cause, claims asserted by any assignees or purchasers of the Banks' loan participation interests are also dismissed. *Condren, Walker & Co., Inc.*, 48 A.D.3d at 331 ("[a]n assignee stands in the shoes of its assignor, subject to all the equities and burdens attached to the property acquired").

IV. **Fraud Claims Asserted on Behalf of PBGC (mot seq 022)**

Defendants argue that the claims asserted on behalf of the Pension Benefit Guaranty Corporation should be dismissed, because Plaintiff cannot establish proximate cause, reliance, or damages, and based upon *in pari delicto*. Defendants also argue that these claims should be dismissed for lack of standing and as preempted by the Employee Retirement Income Security Act (ERISA).

A. *The PBGC and Plaintiff's Allegations*

The Pension Benefit Guaranty Corporation is a United States government corporation and agency. "The PBGC administers and enforces Title IV of ERISA," which "includes a mandatory Government insurance program that protects the pension benefits of over 30 million private-sector American workers who participate in plans covered by the Title." *Pension Benefit Guar. Corp. v. LTV Corp.*, 496 U.S. 633, 637 (1990). The Amended Complaint alleges that the PBGC insured the RGH Pension Plan and the RIC Retirement plan (together, "Pension Plans"), and that RGH and RIC established trusts that would be funded by each company to cover its pension liabilities for the companies' respective plans ("Plan Trusts").

Plaintiff alleges that the PBGC's Department of Insurance Supervision and Compliance ("PBGC DISC") monitors the financial strength of pension plans, relying on publicly-filed financial reports such as the reports prepared by Defendants herein. Plaintiff claims that, if necessary, "available courses of action" for PBGC DISC include terminating a pension plan "so that no additional pension liabilities will accrue," and "working with the company to ensure that it will meet its pension liabilities as they accrue and/or impos[e] liens upon Reliance's collateral in order to decrease the overall amount of pension liabilities that the PBGC will ultimately have to cover." (Am. Compl. ¶ 93.)

According to Plaintiff, in the spring of 2000, PBGC DISC became aware that Reliance had sold certain subsidiaries while retaining responsibility for those subsidiaries' pension plans, and PBGC DISC began to monitor the day-to-day activities of Reliance, including the Form 10-K for the year ending December 31, 1999, which included the financial reports prepared by Defendants. Plaintiff claims that, based upon these reports, "the PBGC did not exercise its power to impose liens or terminate RGH and RIC's Pension Plans. As a result, liabilities continued to accrue for approximately twelve months until Reliance's true financial condition was revealed." *Id.* ¶ 95. Plaintiff avers that, because Reliance was insolvent, it was unable to continue meeting its pension funding obligations, rendering the PBGC responsible for these liabilities. The PBGC allegedly took over the Plan Trusts after RGH and RFS declared bankruptcy in June 2001, and after the Pennsylvania Insurance Department ordered RIC into liquidation in October 2001. (Am. Compl. ¶ 96.) Plaintiff claims that the PBGC ultimately filed proofs of claim for losses totaling $174,642,128 in pension liabilities. *Id.* ¶ 97.

[* 44]

B. *Defendants' Prima Facie Showing on Proximate Cause*

Defendants argue that Plaintiff's claims concerning the PBGC should be dismissed, because any claimed loss causation is based upon speculation. In support of their argument, Defendants submit documentary evidence and the deposition testimony of PBGC's attorneys, John Menke ("Menke") and Stanley Hecht ("Hecht").

1. Relevant Facts

The PBGC began monitoring Reliance in July 2000, after Standard & Poor's lowered Reliance's ratings. (Menke Tr., Dell Affirm. Ex. 116 at 58-59; Flemming Affirm. Ex. 67 at CR06249.) In an internal "Transaction Under Review Memorandum," dated July 24, 2000, the PBGC reported that "Reliance itself appears to be headed towards receivership." *See* Dell Affirm. Ex. 117, at CR06254; Ex. 116, at 94-95; *see also* Dell Affirm. Ex. 172, at 15-16 (Pennsylvania Insurance Department testimony that, when A.M. Best lowered Reliance's rating in June 2000, "the company could no longer sell in the marketplace," which "destroy[ed] . . . the going concern franchise"). The PBGC testified that Reliance continued to accrue pension liabilities while Defendants' alleged misrepresentations went undetected (Dell Affirm. Ex. 116 at 216-217), but that "terminating the plan would have forced a bankruptcy and a receivership just by itself," which "would have tanked the company" and was "something [the PBGC] would have been extremely reluctant to do absent a very special stimulus." *Id.* Ex. 118 at 118-119, 121; *see also* Menke Tr., Dell Affirm. Ex. 116 at 136.

On August 14, 2000, RGH filed its 10-Q for the second quarter of 2000, reporting:

> (1) that the company had an after-tax net loss of approximately $504 million for the quarter; (2) that actuarial net loss reserves were being increased by $444.2 million; (3) that Best's downgrading of RIC's rating during the quarter (from "A-" [Excellent] to "B++" [Very Good] and then to "B" [Fair]) was believed to "seriously impair [RIC's] ability to write many of its lines of business," as a result of which Reliance had entered into agreements to sell much of its property and casualty businesses and had written off its remaining $195.6 million goodwill balance; and (4) that, as a result of the Best downgrade, RGH "d[id] not expect to be able to obtain regulatory approval for dividends from [RIC] sufficient to fund the repayment at maturity of [RGH's] bank debt and the senior notes.
>
> The August 14th 10-Q also warned, ominously:
>
> The Company is in discussions with its creditors and regulators to develop a comprehensive plan to restructure its outstanding debt. However, there can be no assurance that its efforts will be successful. The Company is exploring a full range of alternatives to restructure its debt, among which would be to seek protection under the Federal Bankruptcy Code, which could be in conjunction with a negotiated settlement in advance of filing.

RGH Liquidating Trust, 71 A.D.3d at 202.

On August 17, 2000, Reliance entered into a letter agreement with the Pennsylvania Insurance Department, whereby the Pennsylvania Insurance Department obtained additional oversight of Reliance's business operations and run-off. (Dell Affirm. Ex. 46; Ex. 116 at 125-127; Ex. 172 at 13-15.) In an internal memorandum dated August 24, 2000, the PBGC stated that Reliance was "no longer functioning as an ongoing concern" and "unable to pay debt obligations . . . and may seek bankruptcy protection," and that one of its pension plans was only 57% funded with $91 million in unfunded benefit liabilities. (Dell Affirm. Ex. 120; Ex. 116 at 123-125.)

On September 7, 2000, a PBGC financial analyst concluded that "RGH appears to be on the verge of bankruptcy," and requested that an internal attorney be assigned to the case. (Dell Affirm. Ex. 121; Ex. 116 at 127-130.) Also in September of 2000, Hecht concluded that Reliance was "deeply troubled," with bankruptcy and Reliance being placed in receivership as "distinct possibilities," and that "it was a case that one way or the other would likely result in . . . termination [of] two pension plans." (Dell Affirm. Ex. 118 at 22-25, 52.) Also in September 2000, RGH and RIC notified the PBGC of a "reportable event" under ERISA, as a result of a reduction in the number of active participants in a defined benefit plan. (Dell Affirm. Ex. 122; Ex. 116 at 131-132.)

On October 4, 2000, Hecht sent an internal email to a PBGC financial analyst concerning the "Reliance 10K," stating that Hecht "looked at securities disclosures" and concluded that the "state regulator pretty severely limits what can be upstreamed to the parent." (Dell Affirm. Ex. 123; Ex. 118 at 83.) As discussed above, on October 23, 2000, Reliance announced that it was increasing its loss reserves by approximately $332 million, with the aggregate loss reserve increase now totaling more than $800 million. On November 16, 2000, Standard & Poor's lowered RGH's ratings from "double-'C'" to

"'D,'" and on December 1, 2000, A.M. Best downgraded Reliance to "D (Poor)." (Dell Affirm. Exs. 152 and 153.) An internal PBGC email, dated November 30, 2000, acknowledged that RIC's statutory surplus had been reduced to $650 million. (Dell Affirm. Ex. 126.) By mid-December, RGH's stock was trading at less than $1 per share, and stock trades were suspended by the New York Stock Exchange. (Dell Affirm. Ex. 127; Ex. 116 at 139, 148-149.)

In an internal PBGC email, dated December 4, 2000, Hecht stated: "It is pretty clear that they [Reliance] are operating in a total crisis mode, with bankruptcy looming for the holding companies and maybe receivership for the subs." (Dell Affirm. Ex. 128, at CR06307; Ex. 118 at 96-97.) Menke testified that, at this time, the PBGC knew Reliance had increased loss reserves by more than $800 million and that its stock was trading below one dollar, but the PBGC nevertheless had not commenced proceedings to terminate the Pension Plans. (Dell Affirm. Ex. 116 at 135-136.) Menke stated that "there was still hope that they [Reliance] would be able to meet their obligations to their pension plans at this time." *Id.* at 136. According to Menke, "[t]ermination of the pension plans is a last resort thing, all other available possibilities mostly have to be gone before PBGC seeks to terminate a pension plan." *Id.* Menke stated that "there was still some hope, perhaps though flagging, that the insurance company would be able to both pay policies holders and have sufficient resources left to meet its obligations to its other creditors, including its pension plans." *Id.* at 137.

On January 29, 2001, the Pennsylvania Insurance Department placed RIC under formal supervision. (Dell Affirm. Ex. 129 at CR06750; Ex. 118 at 132.) In May 2001, the PBGC received an Associated Press article stating that, for the year 2000, Reliance was posting losses of $2 - $2.2 billion, and that it would have to increase its loss reserves by $1 - $1.2 billion. (Dell Affirm. Ex. 130.) The article stated that Reliance's surplus totaled only $624 million when it was last reported, on September 30, 2000, "raising the possibility of a multimillion-dollar shortfall." *Id.* By order dated May 29, 2001, the Pennsylvania Insurance Department placed RIC into rehabilitation. (Dell Affirm. Ex. 131.)

In September 2001, the Pennsylvania Insurance Department recommended that the PBGC take over RIC's pension plan, but the PBGC did not do so at that time, even though RIC had missed a minimum funding contribution that month. (Dell Affirm. Ex. 132; Ex. 116 at 111, 147-149.) By order dated October 3, 2001, the Pennsylvania Insurance Department terminated the rehabilitation of RIC, declared it insolvent, and placed the company into liquidation. *Id.* Ex. 133. By letter dated October 10, 2001, the Pennsylvania Insurance Department's counsel requested that the PBGC terminate RIC's retirement plan. *Id.* Ex. 134.

Menke testified that, as of December 2000, there was "hope" that Reliance would pay policy holders and creditor obligations, and that "[t]hat hope ended effectively when the insurance company was put into liquidation" in "September, October 2001." (Dell Affirm. Ex. 116 at 136-137.) Yet, notwithstanding the foregoing evidence, the PBGC did not terminate RIC's retirement plan until several months later, on February 28, 2002. (Dell Affirm. Ex. 135.) The PBGC did not terminate RGH's pension plan until two years later, on January 31, 2004. *Id.* Ex. 136. Menke testified that the PBGC team working on the Reliance matter decided not to recommend termination of RGH's pension plan in January 2002, even though RGH was in bankruptcy, had only two remaining employees, was in liquidation, and "no one imagined that they had any money to put into the pension plan at that point in time." (Dell Affirm. Ex. 116 at 190-191, 505-506.)

Significantly, Menke testified that he could only speculate as to whether an increase in loss reserves would have led the PBGC to terminate the Pension Plans earlier. (Dell Affirm. Ex. 116 at 137-138, 210-211, 213-214, 225-226; Flemming Affirm. Ex. 65 at 476-477, 479.) Hecht testified that he did not know whether the PBGC would have done anything differently if loss reserves were increased by over $400 million at the end of 1999 instead of in June 2000. (Dell Affirm. Ex. 118 at 144-146.) Hecht testified that, even if loss reserves were increased by over $1 billion, the PBGC "was a little bit hamstrung in terms of what it could do" if Reliance was current on its contributions. *Id.*

at 151-153, 155-156. Hecht also testified that, if Reliance had reported a statutory surplus of $650 million, he "doubt[ed]" it would have "affect[ed] anything [he was] doing." *Id.* at 163.

2. Analysis

The foregoing evidence makes a prima facie showing that Defendants' financial reports did not proximately cause the PBGC's injury, that the financial reports were not "a substantial factor in inducing the [PBGC] to act the way it did," and that Plaintiff's allegations are based upon speculation as to whether the PBGC would have terminated the Pension Plans earlier and the mere possibility of loss causation, all of which support Defendants' motion for summary judgment dismissal. *Curiale*, 214 A.D.2d at 27; *Starr Found.*, 76 A.D.3d at 27, 28; *Nicosia*, 77 A.D.3d at 456; *Geary v. Hunton & Williams*, 257 A.D.2d 482, 482 (1st Dep't 1999) (dismissing fraud claim where damages were "speculative and undeterminable"); *Shea*, 244 A.D.2d at 46-47; *Silva*, 251 A.D.2d at 945.

C. *Plaintiff's Rebuttal on Proximate Cause*

"Affording plaintiff[], nonmovant[], the benefit of all reasonable inferences in [its] favor," as is required on a summary judgment motion, *Dabbagh v. Newmark Knight*

Frank Global Mgt. Serv., LLC, 99 A.D.3d 448, 449 (1st Dep't 2012), Plaintiff fails to raise a factual issue for the following reasons.

Plaintiff refers to the Banks' opposition argument, claiming that the misrepresentations in Defendants' financial reports caused the PBGC to refrain from acting on opportunities available to it, such as terminating the Pension Plans. In support of this argument, Plaintiff cites to Menke's deposition testimony, stating that there are certain "triggering event[s]" that could cause the PBGC's financial analysts to look up a company's available financial information. (Flemming Affirm. Ex. 65 at 408-410, 481-482.) Menke explained that news articles, or publicly filed audit opinions indicating that "there was a going concern issue with the company," would cause the PBGC to "immediately begin to monitor that company seriously." *Id.* at 410-412.

Here, Plaintiff submits a July 6, 2000 news article, announcing that Standard & Poor's lowered RGH's rating, which triggered the PBGC to assign a financial analyst to monitor RGH. (Flemming Affirm. Ex. 67.) The PBGC analyst, in turn, prepared the July 24, 2000 "Transaction Under Review Memorandum," analyzing RGH's financial condition, including RGH's 1999 Annual Report ("TUR Memorandum"). (Flemming Affirm. Ex. 65 at 418-426; Ex. 69; Ex. 72.) Included in the 1999 Annual Report was Deloitte's "Independent Auditors' Report," stating that, in Deloitte's opinion, RGH's "consolidated financial statements present fairly, in all material respects, the financial position of [RGH] and subsidiaries as of December 31, 1999." *Id.*, Ex. 72 at 9573. The TUR Memorandum appears to have been created based upon the PBGC's review of RGH's 1999 Annual Report, and possibly the PBGC's review of the Independent Auditors' Report contained therein. Plaintiff argues that, if Reliance's financial condition were accurately reported by Defendants, the PBGC would have commenced monitoring Reliance four months earlier than the July 2000 TUR Memorandum. (Pl.'s Opp. Br. at 112.) According to Plaintiff, "it is reasonable to infer that the PBGC would have accomplished the termination of the pension plans up to 19 months earlier, rather than commencing the process of doing so in October 2001." *Id.*

As a preliminary matter, the TUR Memorandum acknowledged RGH's dire financial condition notwithstanding the purported misrepresentations in the Defendants' financial reports. Specifically, the memorandum stated that RGH "has been in a downward spiral" since 1999, that Leucadia backed out of the purchase of Reliance stock, that the rating agencies downgraded Reliance, and that Reliance divested "its most profitable businesses." *Id.*, Ex. 69 at CR06253-CR06254. The memorandum also acknowledged that "Reliance itself appears to be headed towards receivership. If the pension plan is underfunded on a termination basis and remains with Reliance, PBGC could reasonably expect to experience long run loss." *Id.* Notwithstanding this information, and its subsequent knowledge of Reliance's deteriorating financial condition, the PBGC refrained from terminating the Pension Plans.

In any event, as discussed above, even if the PBGC began monitoring Reliance earlier, the PBGC could only "speculate" whether it would have terminated the Pension Plans earlier but for Defendants' misrepresentations. In response to Defendants' Rule 19-a Statement that "[t]here is no evidence as to when the PBGC would have terminated the [Pension] Plans in the 'but for' world," Plaintiff concedes that this contention "would require the PBGC to *speculate* what it would have done with proper information in real time and when it would have done it, a circumstance with which it was not presented . . ." Defendants' and Plaintiff's Rule 19-a Statement, ¶ 128 (emphasis added). In short, Plaintiff fails to "come forward with a nonspeculative basis for determining how accurate disclosure" of the financial statements would have affected the PBGC's decision to terminate the Pension Plans earlier. *Starr Found.*, 76 A.D.3d at 27; *Geary*, 257 A.D.2d at 482; *see also Herbert H. Post & Co. v. Sidney Bitterman, Inc.*, 219 A.D.2d 214, 224 (1st Dep't 1996) ("Plaintiff must establish, beyond the point of speculation and conjecture, a causal connection between its losses and the defendant's actions").

Furthermore, as discussed above, Hecht testified that, if Reliance had reported a statutory surplus of $650 million at the end of 1999, instead of on November 30, 2000, he "doubt[ed]" it would have "affect[ed] anything [he was] doing." (Dell Affirm. Ex. 118 at

163; Ex. 126.) Thus, Plaintiff does not dispute that the PBGC did not terminate the Pension Plans even upon discovering that Reliance's surplus had been overstated by more than $500 million, and that Reliance was in dire straits financially, headed towards receivership, considering bankruptcy, and no longer operating as a going concern. (Pl.'s Rule 19-a Response ¶ 72.)

Nor does Plaintiff dispute that the PBGC refrained from terminating the Pension Plans when RGH and RFS filed for bankruptcy. *Id.* Plaintiff's evidence fails to raise an issue of fact as to whether the PBGC would have terminated the Pension Plans earlier, but for Defendants' misrepresentations. Nor is there a factual issue as to whether the PBGC would have imposed liens on Reliance's collateral, as is alleged in the Amended Complaint (Am. Compl. ¶ 93), as the PBGC testified that liens never arose because Reliance remained current in its pension plan contributions. (Dell Affirm. Ex. 118 at 55-57.) If anything, the evidence shows that the PBGC would not have terminated the Pension Plans regardless of Defendants' financial reports. At most, Plaintiff offers a speculative theory of the PBGC's early termination, which is insufficient to raise a factual issue. *Starr Found.*, 76 A.D.3d at 27; *Geary*, 257 A.D.2d at 482.

Plaintiff's argument relies upon the same legal authority as it did in opposition to the Banks' motion, including *In re Refco Sec. Litig.*, 2012 WL 607612, 2012 US Dist

LEXIS 25661, and *AUSA Life I.* For the same reasons discussed above, these cases do not raise a factual issue or warrant a different result.

D. *Conclusion*

For the foregoing reasons, Defendants' motion for summary judgment dismissing the Amended Complaint is granted with respect to claims involving the Pension Benefit Guaranty Corporation. Because summary judgment dismissal is granted on the merits on the element of proximate cause, the court does not address Defendants' remaining arguments.

V. <u>Fraud Claims Asserted on Behalf of Woodward and Howard (mot seq 023)</u>

Defendants argue that the fraud claims asserted on behalf of Woodward and Howard should be dismissed because Plaintiff cannot establish the elements of reliance or proximate cause. Defendants also argue that these claims should be dismissed, based upon *in pari delicto* and due to spoliation.

The Amended Complaint alleges that Defendants' misrepresentations assured Woodward and Howard (former employees of Reliance Group Holdings and Reliance Financial Services) of the companies' solvency. (Am. Compl. ¶¶ 98-99.) Plaintiff claims that the financial reports prepared by Defendants persuaded these employees to refrain from cashing out their pension and employee benefits, and that once the companies' true financial condition was revealed, RGH and RFS were unable to pay out the obligations owed to these employees. *Id.*

A. *Woodward's Reliance*

Woodward testified that he did not recall whether he relied on Reliance's 1999 Form 10-K, and that he never saw the auditor's opinion, Form 10-K, or statement of actuarial opinion prepared by Defendants. (Dell Affirm., Ex. 160, at 15, 28-32, 128.) Woodward testified that he neither read Reliance's Form 10-K in 2000 nor personally relied on the 10-K in making his decision about the pension plan. *Id.* at 114. This testimony establishes that Woodward did not personally rely on the financial reports prepared by Defendants.

Woodward testified that, sometime in March of 2000, he attended a meeting with his former employer, Nelson Hurst, an insurance broker that occasionally placed insurance business with Reliance. *Id.* at 16-17, 19. The purpose of that meeting was to assure Nelson Hurst clients that their insurance was being placed in viable markets, but Woodward conceded that Nelson Hurst was not authorized to speak on behalf of Deloitte or Reliance. *Id.* at 18-19. Woodward did not recall whether anything was said at the Nelson Hurst meeting about Reliance's reserves, and Woodward did not know whether

Nelson Hurst had reviewed Reliance's 1999 Form 10-K prior to this meeting. *Id.* at 21-22, 27-28, 39, 44, 46. Nor did Woodward recall whether there was any reference to the Form 10-K or Lommele's statement of actuarial opinion at the meeting. *Id.* at 28-31. Woodward testified that he believed Nelson Hurst had reviewed Reliance's 1999 Annual Report, but he did not recall any reference to this document. *Id.* at 29-30.

Woodward testified that he was not sure he relied on Nelson Hurst's analysis, but rather, he testified: "I relied on my own judgment. That's all I relied on. But to reach a judgment I listened to what Nelson Hurst had to say." *Id.* at 33, 40; Ex. 159, at 85. Woodward also testified that, "[i]f it was good enough for my old company, it was good enough for me." (Flemming Affirm. Ex. 95 at 85.) Woodward conceded that Deloitte "made no statements to [him]," but claims that he believed "Reliance was a company in good standing" based on its "clean" audit opinion. *Id.* at 69; Ex. 98 at 33-34, 37-38.

In support of its reliance argument (vis-à-vis the Nelson Hurst meeting), Plaintiff cites to *Tindle v. Birkett*, 171 N.Y. 520 (1902). In *Tindle*, the defendant made and delivered to ratings agencies written statements that misrepresented the defendant company's financial condition to obtain favorable credit ratings. The defendant knew that "the credit of the firm was so rated in the reference books sent by [the ratings] agencies to merchants and business people." *Id.* at 523. In *Tindle*, it was undisputed that "[t]he plaintiffs had and used" the ratings in their business. *Id.* The Plaintiffs "reli[ed] on the correctness of the rating, without any other knowledge, sold and delivered the goods in question upon credit," but "[t]he statements upon which these ratings were given . . . were grossly false." *Id.* Here, conversely, Woodward testified that he never had or used the financial statements prepared by Defendants. As discussed above, Woodward did not rely upon the "correctness" of Defendants' reports, but rather, he either relied upon his own judgment, or upon the judgment of Nelson Hurst, with no knowledge as to Nelson Hurst's reliance on the financial statements prepared by Defendants. Therefore, *Tindle* is distinguishable on its facts.

Although Plaintiff's claims are based upon Defendants' misrepresentations, the evidence establishes that Woodward "did not specifically know of any of them," and he "cannot claim reliance on alleged misrepresentations of which [he] was unaware even by implication." *Securities Inv. Protection Corp. v. BDO Seidman*, 95 N.Y.2d 702, 710 (2001). Woodward conceded that he had no way to "sort between what Nelson Hurst said [at the March 2000 meeting] and what the underlying documents that Nelson Hurst read in conveying the information to [Woodward] said," which is insufficient to establish the element of justifiable reliance. *See* Dell Affirm. Ex. 160 at 111-112; *Securities Inv. Protection Corp.*, 95 N.Y.2d at 711 (where accountant's reports "were filtered through the NASD's own process of evaluation, [the plaintiff] cannot claim justifiable reliance on the filtered statements, or the absence thereof, as representing either the sum or substance of [the accountant's] representations"). In any event, any assumptions by Woodward as to Nelson Hurst's reliance upon the financial reports prepared by Defendants is insufficient to raise a triable issue on summary judgment. *Smith v. Johnson Prods. Co.*, 95 A.D.2d 675, 676 (1st Dep't 1983) ("reliance upon surmise, conjecture or speculation" insufficient to raise a factual issue).

Moreover, Woodward could not recall whether the meeting with Nelson Hurst was "early March or late March," making it impossible to determine whether any such reliance could have been based upon Defendants' misrepresentations, as their financial reports were not made public until the March 30, 2000 filing of Reliance's Form 10-K. Dell Affirm. Ex. 160 at 16, 115, 119; *see Callisto Pharm., Inc. v. Picker*, 74 A.D.3d 545, 545-546 (1st Dep't 2010) ("[t]here is no evidence, other than plaintiff's speculation, that defendant was negotiating during the two companies' ultimately fruitless discussions"); *Abrahami v. UPC Constr. Co.*, 224 A.D.2d 231, 233 (1st Dep't 1996) ("loose, equivocal or contradictory" evidence insufficient to prove fraud).

Although Woodward did not recall any reference to Reliance's 1999 year-end financials, he testified that any such audit opinion would be referenced only if it were qualified. (Dell Affirm. Ex. 160 at 30-31.) In essence, Woodward claims that he relied upon Reliance's "clean opinion" and "what Deloitte had not said." (Flemming Affirm. Ex. 95 at 69; Ex. 98 at 33.) However, "'no news is good news' is an insufficient basis for [plaintiff's] fraud claim here." *Securities Inv. Protection Corp.*, 95 N.Y.2d at 709. In other words, Plaintiff cannot establish Woodward's reliance by assuming that Nelson Hurst's "silence" meant that Defendants had given Reliance "a clean bill of health." *Id.*

For the foregoing reasons, Defendants have shown that Woodward did not rely on the financial reports prepared by Defendants. In opposition, Plaintiff fails to raise a factual issue. Accordingly, Defendants' motion for summary judgment is granted and the fraud claims are dismissed to the extent asserted on behalf of Woodward. *Securities Inv. Protection Corp.*, 95 N.Y.2d at 709 ("[p]laintiff cannot sustain a cause of action for fraud if defendant's misrepresentation did not form the basis of reliance").

B. *Howard's Reliance*

Howard testified that she "never saw any statements by Deloitte," including the 1999 financial statements and statement of actuarial opinion prepared by Defendants, and that she did not rely on them. (Dell Affirm. Ex. 161, at 22-25, 43-44; Ex. 158 at 22-24, 50-51.) Howard could not recall why she refrained from selling her RGH stock. *Id.* Ex. 158 at 30-31. Howard testified that she "probably" read the 1999 Annual Report based on the fact that she "read all the annual reports," although admittedly "not from cover to cover." (Flemming Affirm. Ex. 34 at 23.) However, Howard immediately clarified this equivocal testimony, stating that she could not specifically recall reading the document (*id.* at 23-25), and then reiterating that she stayed with Reliance based upon promises from management concerning her employment and severance package. *Id.* at 25; *see also* Dell Affirm. Ex. 161 at 15-17, 23; Ex. 158 at 18-19, 24, 35-37, 45; Ex. 164 (notarized letter to Howard from Saul Steinberg, RGH's chairman, stating that "[t]his letter confirms in writing my verbal promise to you that you will have a position with me for the next four years, starting January 1, 2001 at your current salary of $117,400 per year").

This evidence establishes that Defendants' misrepresentations did not form the basis of Howard's reliance. *Securities Inv. Protection Corp.*, 95 N.Y.2d at 709; *Vermeer Owners v. Guterman*, 78 N.Y.2d 1114, 1116 (1991) (dismissing fraud claim where "[n]othing in th[e] record establishes that plaintiffs in fact relied on any misrepresentation by defendants to their detriment"). Accordingly, Defendants' motion for summary judgment dismissing the fraud claims, to the extent asserted on behalf of Howard, is granted.

Because the fraud claims relating to Woodward and Howard are dismissed for lack of reliance, the court does not address Defendants' remaining grounds for dismissal, including proximate cause, *in pari delicto*, and spoliation.

[* 62]

Conclusion

Accordingly, it is hereby

ORDERED that Defendants' motions for summary judgment (motion sequence numbers 021, 022, and 023) are granted and the Amended Complaint is dismissed with costs and disbursements to Defendants as taxed by the Clerk upon the submission of an appropriate bill of costs; and it is further

ORDERED that the Clerk is directed to enter judgment accordingly.

This constitutes the decision and order of the Court.

Dated: New York, New York
June 6, 2013

ENTER:

Eileen Bransten

Hon. Eileen Bransten, J.S.C.