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CDO Disclosures Don't Preclude Citi Fraud Claim: N.Y. Appeals Court.

NEW YORK (Reuters) – A state appeals court on Thursday denied Citigroup Inc's bid to dismiss a fraud claim in a lawsuit stemming from nearly \$1 billion of collateralized debt obligations.

The Appellate Division, First Department, said that disclaimers and disclosures in marketing materials for the securities did not bar plaintiff Loreley Financing from establishing that it relied on Citi's allegedly false and misleading misrepresentations when it bought the securities in 2006 and 2007.

"We find that these disclaimers and disclosures fall well short of tracking the particular misrepresentations and omissions alleged by plaintiffs," Justice Dianne Renwick wrote for a unanimous panel.

Loreley, a group of special-purpose entities formed to invest in CDOs, sued Citi in 2012 for defrauding it into purchasing "fraudulent investments that are now worthless," according to the complaint.

The suit, filed in Manhattan Supreme Court, claimed Citi used the CDOs to offload risks of toxic mortgage-backed securities and to help preferred clients short the housing market. It accused Citi of fraud, rescission, fraudulent conveyance and unjust enrichment.

In June 2012, Citi moved to dismiss the complaint.

In December 2012, Justice Jeffrey Oing granted Citi's motion to dismiss the rescission and fraudulent conveyance claims, but denied its bid to dismiss the fraud and unjust enrichment claim.

On appeal, Citi argued that the marketing materials for the securities required purchasers to disclaim reliance on Citi's advice or representations. The materials, Citi said, warned buyers that collateral underlying the securities was subject to risks and that Citi and its affiliates could act in numerous capacities in the deal that could conflict with buyers' interests.

The First Department disagreed, citing its decision earlier this year in *Basis Yield Alpha Fund v. Goldman Sachs Group*, a CDO lawsuit which it said included "indistinguishable" allegations of fraud.

In that case, the First Department said it affirmed a lower court's decision denying Goldman's bid to dismiss the case based on "very strongly-worded disclaimers and disclosures."

"Basis Yield ... constitutes clear precedent that compels us to find that Citigroup's disclaimers and disclosures do not preclude, as a matter of law, a claim of justifiable reliance on the seller's misrepresentations or omissions," Renwick wrote.

The First Department did dismiss the unjust enrichment claim, however.

Justices Angela Mazzairelli, John Sweeny, Helen Freedman and Judith Gische joined Renwick in the decision.

“Loreley is very pleased with the First Department’s ruling today, and we look forward to presenting our case to the trial court,” said Sheron Korpus, a partner with Kasowitz, Benson, Torres & Friedman who represented Loreley.

Susanna Buergel, a partner with Paul, Weiss, Rifkind, Wharton & Garrison who represented Citi, did not immediately respond to a request for comment.

The case is Loreley Financing et al v. Citigroup Global Markets Inc et al, New York State Supreme Court, Appellate Division, First Department, No. 11886.

For Loreley: Sheron Korpus of Kasowitz, Benson, Torres & Friedman.

For Citi: Susanna Buergel of Paul, Weiss, Rifkind, Wharton & Garrison.

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